REPORT OF COMMITTEE ON INDIAN EXCHANGE AND CURRENCY, 1919.

TO THE RIGHT HON. EDWIN S. MONTAGU, M.P., SECRETARY OF STATE FOR INDIA.

1. We were appointed, on the 30th May 1919, as a Committee to advise in regard to the future of Indian Exchange and Currency. Our terms of reference were as follows:—

TERMS OF REFERENCE.

"To examine the effect of the war on the Indian exchange and currency system and practice, and upon the position of the Indian note-issue, and to consider whether, in the light of this experience and of possible future variations in the price of silver, modifications of system or practice may be required; to make recommendations as to such modifications, and generally as to the policy that should be pursued with a view to meeting the requirements of trade, to maintaining a satisfactory monetary circulation, and to ensuring a stable gold exchange standard."

INTRODUCTORY.

WITNESSES.

2. We have held 40 meetings and examined 28 witnesses. We have endeavoured to obtain evidence of as widely representative a character as possible. The official side of the case has been placed before us by Sir Lionel Abrahams, K.C.B., Assistant Under-Secretary of State, Mr. F. H. Lucas, C.B., C.V.O., Financial Secretary at the India Office, and Mr. M. M. S. Gubbay, C.S.I., C.I.E., Controller of Currency in India, who, in addition to serving as a member of our Committee, was the accredited spokesman of the Government of India. Sir W. Meyer, G.C.I.E., K.C.S.I., who was Financial Member of the Governor-General's Council in India for practically the whole period of the war, also gave evidence. In addition, we had the advantage of hearing Sir David Barbour, K.C.S.I., K.C.M.G., who occupied the post of Financial Member of the Governor-General's Council from 1887-93, when the policy of closing the Indian mints to the free coinage of silver was adopted, and subsequently served as a member of the Indian Currency Committee presided over by Sir Henry Fowler (later Lord Wolverhampton) in 1898-99.

In order to ensure that all important representative associations in India should be given the fullest opportunity to nominate witnesses, we requested the Government of India, through the Secretary of State, to renew the invitation they had issued prior to our first meeting, and to facilitate the deputation of witnesses to this country. The majority of the Chambers of Commerce and other representative associations in India elected to submit their views in writing rather than depute a witness for the purpose. All the memoranda received from them will be found in the volumes of our proceedings, and we need scarcely say that we have given them the careful consideration to which the responsibility and experience of their authors entitle them. Witnesses were specially deputed from India on behalf of the Indian Merchants' Chamber and Bureau and the Bombay Mill-owners' Association.

Eight other witnesses representative of financial, commercial, and banking interests in the East appeared before us. Apart from the representatives of the Eastern Exchange Banks Association, these included Lord Inchcape, G.C.M.G., K.C.S.I., K.C.I.E., who served on the Secretary of State's Council from 1897 to 1911; Mr. M. de P. Webb, C.I.E., C.B.E., formerly Chairman of the Karachi Chamber of Commerce; Mr. J. N. Stuart, of the Indian Tea Association; Sir E. Rosling, of the Ceylon Association; Mr. J. F. N. Graham, who represented the Glasgow Chamber of Commerce; and Mr. S. R. Bomanji, member of the Indian Merchants' Chamber and Bureau, Bombay. Invitations were also issued to the East Indian Section of the London Chamber of Commerce and the Manchester Chamber of Commerce, but these bodies did not consider it necessary to nominate a special witness. The Ceylon Chamber of Commerce also found it impossible to depute a representative to give evidence before us.

3. Prior to our appointment the Secretary of State had appointed Professor C. G. Cullis, D.Sc., and Professor H. C. H. Carpenter, F.R.S., of the Imperial College of Science and Technology, to conduct an en-

quiry into the conditions of silver production, the prospects of future output, and the causes by which it was likely to be influenced. We were able to avail ourselves of the result of this valuable investigation, and the two gentlemen who had conducted the enquiry appeared before us. Mr. E. L. de M. Mocatta, partner in the firm of Messrs. Mocatta and Goldsmid, bullion brokers, also gave evidence on the conditions and prospects of the silver market.

We found it necessary to examine the bearing of the exchange value of the rupee on the level of prices in India, and, in response to our request for evidence on this point, the Government of India deputed Mr. K. L. Datta, who in 1910-13 had conducted an enquiry into the rise of prices in India from 1895, to appear before us, not indeed as the official spokesman of the Government, but as an authority on prices and economic conditions in India. We also took evidence from Sir James Douie, K.C.S.I., a retired officer of the Indian Civil Service, and Mr. James Campbell, O.B.E., I.C.S., on this aspect of the case.

Sir Brien Cokayne, K.B.E., Governor of the Bank of England, gave evidence with reference to the Indian demand for the precious metals.

The remaining witnesses were: Mr. F. T. Rowlatt, Governor of the National Bank of Egypt; Mr. F. I. Kent, Director of the Foreign Exchange Section of the Federal Reserve Board of the United States of America; Sir Stanley Reed, K.B.E., Editor of the *Times of India*: Mr. J. M. Keynes, C.B., a Member of the Royal Commission on Indian Finance and Currency, 1913-14; Professor H. Stanley Jevons, of Allahabad University; and Mr. S. K. Sarma, a student of Indian currency questions.

We wish to express our sincere regret at the premature death of Sir Lionel Abrahams, K.C.B., Assistant Under-Secretary of State for India, and our sense of the loss which the public service has suffered in the death of an officer of unrivalled knowledge and experience in all questions connected with Indian currency and finance. Our records show the high value and wide scope of the evidence which we received from him in the course of our enquiry.

SCOPE OF ENQUIRY.

4. At the outset of our Report we would draw particular attention to the last phrase of our reference under which we are directed to make recommendations with a view "to ensuring a stable gold exchange standard." This precluded us from considering the question of returning to a silver standard such as existed before 1893, or of introducing a bimetallic standard. We think it well, however, to add that we are unanimously of opinion that no useful end would have been served by an enlargement of our reference so as to permit the consideration of these alternatives.

5. The history of the Indian currency system from 1893, when the Indian Mints were closed to the free coinage of silver, to 1914, is briefly described in paras. 12—43 of the Report of the Royal Commission on Indian Finance and Currency, which sat in 1913-14 under the chairmanship of the Rt. Hon. Austen Chamberlain, M.P., now Chancellor of the Exchequer. In this report, issued a few months before the outbreak of war, the Commission generally endorsed the policy and measures which had been adopted with a view to the establishment of the exchange value of the rupee on a stable basis. They made important recommendations regarding the use of gold as currency, the minting of gold in India, the development of the note-issue, the utilisation of Government balances in India and England, the sale of drafts on India and London, the constitution and location of the Gold Standard and Paper Currency Reserves, the organisation for the discharge of financial business, at the India Office, and the question of establishing a State or Central Bank in India. These recommendations were under the consideration of the Government of India when the financial and economic upheaval consequent on the outbreak of war supervened, and it was decided to postpone further action until the return of normal conditions. We shall refer in later passages of our Report to those suggestions made by the Royal Commission which more particularly concern our enquiry.

Position at the Outbreak of War.

CURRENCY IN CIRCULATION.

6. At the outbreak of war the main facts of the Indian currency system were as follows:—

The Indian currency consisted of British gold coins, silver rupees, subsidiary coins of silver, nickel, and bronze, and currency notes.

The British sovereign and half-sovereign were unlimited legal tender for 15 and 7½ rupees respectively, and the Government had undertaken by notification to issue rupees to the public in exchange for sovereigns and half-sovereigns at the rate mentioned

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above, being the equivalent of 1s. 4d. per rupee. The rupee (as also the half-rupee) was unlimited legal tender and was the main metallic medium for the transaction of business. Currency notes of denominations of Rs. 5 and upwards were in circulation, and were legal tender without limit of amount. They were redeemable in coin on presentation at the Currency Offices.

Sovereigns had not been minted in India before the war, but the Government of India ordinarily issued them in exchange for rupees or notes in response to any demand from the public, although they had not undertaken to do so. The extent to which gold coin, actually circulated in India before the war is uncertain, but in Bombay and parts of the Punjab its use as currency was not uncommon. In any case, the amount of gold coin absorbed was large, as will be seen from the figures for the five years before the war:—

Absorption of sovereigns and half-sovereigns in India.

	£.
1909-10	2,873,000
1910-11	1,433,000
1911-12	8,887,000
1912-13	11,100,000
1913-14	12,070,000

SALE OF COUNCIL DRAFTS.

7. There was normally a steady demand for remittance to India as the result of a favourable trade balance. This was adjusted partly by the importation of the precious metals, which was unrestricted, and partly by the sale by the Secretary of State in Council of drafts on the Government of India. The sale of these drafts, generally known as Council Drafts, was primarily intended to provide funds for meeting expenditure on behalf of the Government of India in the United Kingdom. It had the effect of releasing currency (metallic rupees or notes or, exceptionally, gold) in India against payment of sterling in London, and it was found convenient to extend the sales so as to provide additional currency in response to the requirements of trade. The same result would have been produced by the shipment of gold to India and its tender to the Government in exchange for rupees; but the acceptance in London of sterling (which was then equivalent to gold) instead of gold in India was convenient both for the Government and for the purchasers of Council Drafts.

REVERSE COUNCILS.

The amount of the Council Drafts offered for sale each week was therefore fixed not only with reference to the requirements of the India Office, but also with reference to the demands for remittance to India, subject always to the capacity of the Government of India's resources to meet them. The rate obtained for the drafts varied from time to time according to trade demand, but as there was a standing offer to sell bills without limit of amount at 1s. 4⅛d. per rupee, the price never exceeded this figure, which corresponded to the theoretical gold export point. The Secretary of State also maintained the practice of not selling his bills below 1s. 3 29-32d. per rupee. If, owing to a temporary change in the normal current of trade, there was a tendency for the exchange value of the rupee to fall below this figure, and if this tendency was not sufficiently counteracted by a cessation of the sales of drafts, the situation was met by the sale in India of bills on London, generally known as "Reverse Councils," at 1s. 3 29-32d. per rupee. The Gold Standard Reserve, which had been accumulated from the profits on the coinage of rupees, was available for the purpose of meeting these Reverse Drafts, thus answering the purpose for which it was created, and preventing any further fall in the exchange value of the rupee.

The effect of these arrangements was to keep the exchange value of the rupee very near to the ratio of 15 rupees to the £. Such fluctuations as occurred were similar to those that occur from time to time in the exchange between gold standard countries where the variations are limited by the cost of moving gold to adjust the balance of indebtedness.

The effective maintenance of this fixed relation depended not upon the import and export of gold, but upon the action of the Secretary of State and the Government of India in giving rupees in exchange for gold or sterling, and sterling for rupee currency, in the manner explained above. The Indian standard of value has therefore been described not as a gold standard but as a gold exchange standard. This designation, however, is open to criticism on the ground that it does not take account of the distinction which it has now become necessary to observe between gold and sterling. This distinction, as we shall see later, introduces a new and critical problem in connection with the exchange.

TRADE BALANCE.

8. The precious metals played a part little less important than that of Council Drafts in the adjustment of India's trade balance. The following table sets forth the balance of trade on private account, the

net imports of treasure on private account, and the sales of Council Drafts for the 10 years prior to the outbreak of war:—

	Excess of Exports over Imports on Private Account.	Net Imports of Treasure on Private Account (Gold & Silver, Coin and Bullion).	Net Sales of Council Drafts (i.e., Council Drafts less Reverse Drafts.)
1904-5 ...	40,548,200	16,700,600	24,150,000
1905-6 ...	39,086,700	9,646,900	31,886,000
1906-7 ...	45,506,600	14,420,000	34,069,400
1907-8 ...	31,640,000	18,253,300	15,676,700
1908-9 ...	21,173,300	11,116,300	5,335,300
Total...	177,954,800	70,137,100	111,117,400
1909-10 ...	47,213,000	20,688,400	27,710,600
1910-11 ...	53,685,300	21,700,000	26,389,800
1911-12 ...	59,512,900	28,706,000	26,917,500
1912 13 ...	57,020,900	29,435,000	25,983,500
1913-14 ...	43,753,900	19,713,000	31,200,800
Total...	261,186,000	120,242,000	138,202,200

It is impossible, however, to arrive at any exact analysis of all the elements contributing to the settlement of India's trade balance, since the "invisible" exports and imports (freights, insurances, interest, transfer of profits, movements of capital, etc.) cannot be valued accurately.

Effect of Outbreak of War.

9. The outbreak of war immediately caused, in India as elsewhere, a general dislocation of trade and business of which the principal symptoms were the weakening of exchange, withdrawals of Savings Bank deposits, a demand for the encashment of notes, and a run on Indian gold stocks.

The weakening of exchange was met by the proved expedient of offering drafts on London. Between 6th August 1914 and 28th January 1915, Reverse Councils were sold to the extent of £8,707,000. In February 1915 the demand for Council Drafts revived, and, apart from further periods of weakness in 1915-16, and between November 1918 and April 1919, when Reverse Councils were sold to the extent of £4,893,000 and £5,465,000 respectively, Indian exchange remained strong throughout the duration of the war.

The net withdrawal of Savings Bank deposits amounted in the first two months of the war to Rs. 6 crores, out of the total deposits of 24½ crores on 31st July, 1914. From September to October, 1914 there were further withdrawals to the extent of Rs. 2 crores. Subsequently there was a recovery, but the net withdrawals for the year 1914-15 amounted to over Rs. 8 crores. The tide turned in 1915-16, and since that date deposits have continued to increase, with the result that the figure at the end of 1918-19 was 18¾ crores. There was also a run on the banks, but this proved of short duration.

ENCASHMENT OF NOTES.

10. Some lack of confidence in the Indian note issue manifested itself at the outbreak of war and resulted in a net return of currency notes to the extent of 10 crores between 31st July, 1914, and 31st March, 1915, at which date the net circulation had declined from Rs. 66.28 crores to Rs. 55.65 crores. The silver held in the Paper Currency Reserve fell from Rs. 33.94 crores on 31st July to Rs. 29.87 crores on 31st December, 1914. But from the spring of 1915 onwards there has been a steady increase of the note circulation and on 30th November, 1919, the net circulation amounted to Rs. 178.93 crores.

At the end of July, 1914, there arose a keen demand for gold in exchange for notes, and between the 1st and 4th of August the Government of India lost about £1,800,000 of gold. Some precautions had been taken to discourage the withdrawal of gold for internal purposes when there was a demand for its use as a means of foreign remittance; but when it was seen that the precautions were unavailing it became necessary on 5th August to suspend the issue of gold to private persons. After that time notes presented for encashment were paid in silver coin only.

The disquieting symptoms to which we have referred lasted only for a short time. The return of public confidence was assisted by the assurance given to the banking and commercial community of adequate and continuous facilities for remittance and by the readiness with which the Government of India met demands for the encashment of currency notes.

Currency Difficulties.

11. It is not surprising that the outbreak of war should have caused a temporary disturbance of Indian financial conditions, but when the first shock had passed away the currency mechanism worked smoothly. It was not until the end of 1916 that acute complications arose in the sphere of Indian currency and exchange. These complications showed themselves mainly in the rapid rise in the price of silver and later in the increasing difficulty of obtaining silver to meet the heavy demands for silver coin. The causes contributing to these results were

various, and it will be necessary to trace them in some detail.

12. The Government of India, as is well known, are under the obligation of meeting heavy sterling payments in the United Kingdom. The net amount of these in the years 1910-14 averaged over £25,000,000 a year. The ability of the Government of India to remit to London the funds required for these payments, and also the successful working of the Indian currency system, depend on the existence of a substantial balance of trade in India's favour. In the period immediately preceding the outbreak of war India had enjoyed a series of remarkably prosperous seasons, as will be seen from the following table, which exhibits the value of her exports and imports on private account for the years 1909-10 to 1913-14:—

Exports and Imports of Merchandise on Private Account.

Year.	Exports.	Imports.	Net Exports
	£	£	£
1909-10 ...	135,253,000	78,040,000	47,213,000
1910-11 ...	139,921,300	86,236,000	53,685,300
1911-12 ...	151,896,100	92,383,200	59,512,900
1912-13 ...	164,361,800	107,343,900	57,020,900
1913-14 ...	165,919,200	122,165,300	43,753,900
Average for 5 years ...	149,470,900	97,233,700	52,237,200

The corresponding figures for the years 1914-15 to 1918-19 are as follows:—

Year.	Exports.	Imports.	Net Exports
	£	£	£
1914-15 ...	121,061,100	91,952,600	29,108,500
1915-16 ...	131,586,800	87,560,200	44,026,600
1916-17 ...	160,591,200	99,748,000	60,843,200
1917-18 ...	161,700,000	100,280,000	61,420,000
1918-19 ...	169,230,400	112,690,000	56,540,000
Average for 5 years.	148,833,800	98,446,100	50,387,700

It will be observed that the average balance in India's favour was slightly higher in the earlier quinquennium than in the later, mainly owing to the heavy fall in the first two years of the war. But if we take the three years 1916-17, 1917-18, 1918-19, when Indian currency difficulties were most acute, the average balance of trade in India's favour, viz., £59,601,100, will be seen to have been decidedly in excess of the average of the last three years of the pre-war period (1911-12 to 1913-14), viz., £53,429,200. During the war imports into India were limited by the restriction of the available supplies from manufacturing countries in Europe. Imports from Germany and Austria ceased entirely on the outbreak of war, whilst the productive power of the United Kingdom and her Allies was more and more completely absorbed on war industries as hostilities were protracted. There was consequently a large reduction in the quantity of goods imported into India, and it was only the rise in prices that maintained the value of the import trade and prevented its actual contraction. Exports from India, on the other hand, though restricted by difficulties of transport and finance, were in great demand. Supplies of raw materials and foodstuffs were required for the use of the Allied Powers, and the prices they realised were abnormally high. Enhanced values counteracted the shortage of freight and restrictions of finance, with the result already indicated, that the favourable trade balance was not only maintained, but even showed a tendency to increase.

EXCEPTIONAL DISBURSEMENTS.

13. The large balance of trade indebtedness in India's favour was reflected in the strength of exchange and the heavy demand on Government for currency; and other special causes were at work during the war to intensify this demand. India formed the base of important military operations in Mesopotamia, Persia and East Africa. The Government of India were called upon to provide funds for the payment of British and Indian troops engaged, for the purchase of a large part of the supplies, and for other expenses incidental to a modern campaign, and also for meeting civil expenditure in occupied territory. The amount of the recoverable expenditure incurred by the Government of India on behalf of the Imperial Government between 1914 and the present date has exceeded £240,000,000, and expenditure of this nature has not yet ceased. In addition to the above, arrangements were made for the financing of purchases in India on behalf of certain Dominions and Colonies and for the provision of rupee credits, amounting to 20 crores in 1917-18 and 1918-19, for American importers of Indian produce.

These exceptional disbursements created a heavy additional demand for Indian currency.

14. We have already referred to the part that the imports of gold and silver into India play in normal conditions in adjusting India's favourable trade balance. We shall deal later with the nature of the Indian demand, monetary, industrial and social, for the precious metals. At present we are concerned with the deficiency in the satisfaction of this demand in the period of the war. The following table exhibits the value of India's imports of gold and silver for the five years 1909-10 to 1913-14, and the corres-

ponding value in the years 1914-15 to 1918-19 :—

Net Imports into India of Treasure on Private Account.

	Gold Coin and Bullion.	Silver Coin and Bullion.	Total.
	£	£	£
1909-10 ...	14,446,000	6,242,000	20,688,000
1910-11 ...	15,986,000	5,714,000	21,700,000
1911-12 ..	25,178,000	3,528,000	28,706,000
1912-13 ..	25,052,000	4,383,000	29,435,000
1913-14 ...	15,550,000	4,163,000	19,713,000
Total ...	96,212,000	24,030,000	120,242,000
1914-15 ...	5,637,000	6,676,000	12,313,000
1915-16 ...	3,267,000	3,717,000	6,984,000
1916-17 ...	2,797,000	—1,440,000	1,357,000
1917-18 ...	14,306,000	971,000	15,277,000
1918-19 ...	15,000	38,000	53,000
Total ...	26,022,000	9,962,000	35,984,000

Several factors contributed to the remarkable decline in the import of the precious metals during the latter period.

The first, and far the most important, factor was the difficulty of obtaining gold. The free market in London, on which India had been able to draw in the past, disappeared on the outbreak of war. Restrictions on the export of gold were imposed by belligerent Governments desirous of maintaining their stocks of the metal for war purposes, and India was accordingly only able to obtain very limited quantities. The relatively high imports in 1917-18, mainly from Japan and the United States, were largely caused by the difficulty of obtaining rupee exchange when the sales of Council Drafts were limited and controlled. The low figure for 1918-19 was mainly due to restrictions placed upon the export of gold from the United States.

SHORTAGE OF SILVER.

15. The dearth of gold created a strong demand for silver. This would have tended normally to increase the private imports of silver, which remained unrestricted until September, 1917. But during this period of the war the silver market was subject to conditions of supply and of demand which severely limited the amount of the metal available for private purchasers.

There was, in the first place, a great shortage of supply. The world's production of silver from 1914 onwards exhibited a marked decline from the production of the preceding years. The question is fully discussed in the Report on the World's Production of Silver by Professors Carpenter and Cullis, which is included in the Appendices to our Report. Their statistics are summarised in the following table :—

Mine production of Silver (in Fine Ounces, 000 omitted).

Years	Canada.	U. S. A.	Mexico.	Rest of World.	Total of World.
1910	39,869	57,590	71,372	57,249	219,089
1911	32,559	61,109	79,033	57,683	230,384
1912	31,956	66,041	74,640	60,423	233,060
1913	31,806	71,210	70,704	57,956	231,676
Average for 4 years 1910-13	32,297	63,987	73,937	58,331	228,552
1914	28,449	69,634	27,547	50,418	176,048
1915	26,628	77,369	39,570	41,180	185,745
1916	25,460	78,775	22,838	48,293	176,456
1917	22,221	70,866	31,214	50,949	175,050
Average for 4 years 1914-17	25,689	7 ,886	30,292	49,210	178,075

Approximately three-quarters of the world's silver is mined in North America and Mexico. The decrease in the Canadian production due to the progressive exhaustion of the Cobalt field was more than compensated by an increase in the production of the United States of America; and the key to the shortage of silver is to be found in Mexico, where, owing to political disturbances, the production of silver fell from an average of 73,937,000 fine ounces for the years 1910-13 to an average of 30,292,000 fine ounces for the years 1914-17, a reduction of 43.6 million ounces out of a total reduction of 50.5 million ounces in the world's production. It will be noted that the fall in Mexican production, though it coincided approximately with the beginning of the war, was not caused by the war, but by internal conditions in Mexico.

HEAVY WORLD DEMAND.

16. Had the world's demand for silver remained normal, the marked decline in supplies from 1914 onwards could hardly have failed to produce a rise in price and must have influenced the quantity of the metal available for India. But actually the world's demand for silver was unusually keen, particularly for coinage. The coinage of the British Empire for example absorbed nearly 108 million fine ounces of silver in the years 1915 to 1918 as against 30.5 million fine ounces in the years 1910 to 1913, and there is evidence that there were similar increases in the silver coinage of other countries.

There has also been a heavy demand for China during the last two years. In the years 1914-17 China was a seller of silver and her net exports of the metal amounted to over 77,000,000 standard ounces. From 1918, on the other hand, China has been a persistent buyer, and in recent months the intensity of her demand has been the domi-

nating feature of the silver market. It is probable that the export of the previous years has now been made good, but so far there is no indication of any slackening in the demand.

17. We have seen that war conditions militated against the normal flow of the precious metals to India, where their import would have assisted in the liquidation of the trade balance in India's favour. The burden of liquidating this balance was thus focussed on the Government of India and took the form of heavy demands for currency. The efforts made to meet these demands are indicated by the fact that between April, 1916 and March, 1919, over 300,000,000 standard ounces of silver1 were bought in the market for coinage in addition to 200,000,000 fine ounces purchased under the Pittman Act (see para. 23) as compared with about 180,000,000 standard ounces between April, 1904 and March, 1907, when the Indian demand was specially heavy and continuous.

RISE IN PRICE.

18. These large purchases, combined with the decrease in the supplies of silver and the increased demand from other quarters, reacted strongly on the price of the metal. In 1915 the highest price of silver in the London market was 27½d. per standard ounce. By April, 1916, it had risen to 35⅝d. and in December had reached 37d. The rise in price continued throughout the first part of 1917 and in August it exceeded 43d. We invite attention to this figure, because it marks the point at which the exchange value of the rupee at 1s. 4d. is equivalent to its bullion value, and it was the rise in the price of silver to this figure and above it that necessitated the alterations in exchange to which we refer in paragraph 22. In September, 1917, the price of silver rose to 55d.

In September 1917, the United States Government instituted control over the trade in silver and prohibited the export of the metal except under licence. The effect of this control was to check the rising tendency of silver prices, and between October, 1917, and April, 1918, the London quotation varied between 41⅞d. and 49¼d. per standard ounce. After the passing of the Pittman Act in April, 1918, (see para. 23), no export licences were granted by the Government of the United States of America except for silver which was bought at 101½ cents, or less, per fine ounce, and was required for purposes connected with the prosecution of the war. Similar measures were adopted by the Canadian Government, and the British Government fixed a maximum price for silver corresponding to the American maximum. These measures had the effect of stabilising the market price of silver at about a dollar per fine ounce, and facilitated purchases for India. Between May, 1918, and April, 1919, the London price for silver ranged between 47¾d. and 50d. per standard ounce. But when in May, 1919, the United States Government and the British Government withdrew control over the silver market, a further rise in price occurred, and in May the London price reached 58d., or more than double the maximum attained in 1915. Since that date, mainly on account of the exceptional demands from China, the price has risen still further and on 17th December stood at 78d. per standard ounce.

INFLUENCE OF DOLLAR-STERLING.

19. It is necessary at this stage to refer to another factor tending to raise the price of silver in the London market. During the war arrangements were concerted between the British and American Governments under which the sterling exchange on America was "pegged" at $4.76 7/16. Government support of exchange was withdrawn on 20th March, 1919, and since that date the London-New York exchange has moved heavily against the United Kingdom. On 17th December the £ sterling was equivalent to only $3.83 as against its par value of $4.8666. As America is the principal source of the world's silver supply, the chief payments for the metal have to be made ultimately in that country. The sterling price of silver accordingly takes account of the state of the London-New York exchange, and any rise or fall in that exchange is reflected in the London price. A fall in sterling exchange has thus the effect of raising the London quotation for silver. For any given sterling value of the rupee there is a corresponding sterling price for silver above which silver for coinage into rupees can only be purchased at a loss. If, without any change in the gold price of silver as measured in dollars, the London quotation should rise in consequence of a fall in the London-New York exchange, purchases of silver for India may be rendered impracticable unless the rupee exchange is raised to redress the fall in sterling. The position may be made clear by an illustration. If the exchange value of the rupee is 2s., the Secretary of State can buy silver for coinage into rupees without loss at 63d. per standard ounce. If the London-New York exchange fell 10 per cent., the sterling quotation for silver would, *ceteris paribus*, react

in proportion, and assuming that the price stood at 63d. before the fall in American exchange, it would rise to over 69d. as the direct consequence of the fall in exchange. If in these conditions the Secretary of State wished to purchase silver for coinage without loss, it would be necessary for the rupee exchange to be raised to about 2s. 2½d.

CURRENCY SYSTEM IMPRACTICABLE.

20. In the circumstances we have described the purchase of silver for coinage was attended with serious difficulty. In paragraph 23 we give details of the purchases made. Though these purchases represent a considerable proportion of the world's annual supply, they were insufficient for the heavy and continuous requirements for silver coin. This fact, taken in conjunction with the rising price at which purchases had to be effected, rendered the maintenance of the pre-war currency and exchange system impracticable. The Secretary of State was unable to maintain his offer to sell Council Drafts without limit of amount, while in view of the rise in the price of silver to a level higher than that which corresponds to a bullion value of 1s. 4d. for the rupee, he was compelled to raise the rate at which he sold the limited amount of Council Drafts which he was able to offer.

These fundamental changes in the system were accompanied by a number of supplementary measures designed to meet special difficulties which arose from time to time. We propose to deal first with the changes in the machinery for regulating exchange, viz., (a) the Government control of exchange and (b) the raising of the rate for the sale of Council Drafts, and then to pass on to the other measures adopted by the Government to conserve their resources and to meet the exceptional demands for currency.

Measures Taken.

(a) CONTROL OF EXCHANGE.

After exchange had recovered from the temporary dislocation consequent upon the outbreak of war, the demand for Council Drafts continued on a normal scale until October, 1916. During November the amount of the weekly sales increased rapidly, and in the first fortnight of December they exceeded £5,000,000. The rupee holding in the Paper Currency Reserve had then fallen to 14 crores, and though there was silver awaiting coinage and the Secretary of State had made large purchases, it was evident that the continuance of sales on this scale would endanger the convertibility of the note issue. To avoid this danger the Council Drafts sold by the Secretary of State were limited from 20th December, 1916, the weekly amount, which varied between 120 lakhs and 30 lakhs, being fixed from time to time mainly on a consideration of the rupee resources of the Government of India. The limitation of the amount of Council Drafts at a time when the demand for remittance to India was exceptionally strong and no adequate alternative method of remittance was available led to a divergence between the market rate of exchange and the rate at which the drafts were sold. It also became evident that the remittance available might be insufficient to finance the whole of the Indian export trade, and it was essential that the exports required for war purposes should not be impeded. It was found necessary, therefore, to introduce certain measures of control. From 3rd January, 1917, Council Drafts were sold at a fixed rate, which at the outset was 1s. 4½d. for immediate telegraphic transfers, and the sale was confined to banks and firms on the "Approved List," which included the chief exchange banks and a few large purchasers of drafts. A little later these banks and firms were required to do business with third parties at prescribed rates and to apply their resources primarily to financing the export of articles of importance to the Allies for the purpose of carrying on the war, a list of which was drawn up by the Secretary of State. An appeal was at the same time addressed to other firms engaged in Indian trade to conduct their remittance transactions through the exchange banks. Further, in order to encourage the exchange banks to buy export bills in excess of their purchases of exchange in the other direction, the Secretary of State insured them against the risk of a rise in exchange, by undertaking to sell to them within a year after the war exchange up to the amount of their overbuying at the rate at which their excess purchases had been made.

This scheme of Government control constituted a complete departure from the system of free and unlimited remittance that prevailed before the war, and was naturally unpalatable to the commercial community. But the evidence we have taken shows that the intervention of Government was regarded as inevitable in the circumstances, and it was due largely to the hearty co-operation of the exchange banks and trading firms with the Government that the market rate of exchange was maintained near the rate at which Council Drafts were sold and the necessary finance was success-

fully provided for the large volume of exports of national importance.

TERMINATION OF CONTROL.

After the conclusion of the armistice the necessity for reserving finance for particular exports ceased. The overbuying guarantee was in due course terminated, and the list of articles to which priority of export finance was given was abolished. On the withdrawal of these restrictions, importers were naturally unwilling to continue incurring loss by effecting homeward remittances through the exchange banks, and a considerable business was transacted between importers and exporters direct at rates appreciably higher than the rate for Council Drafts. Meanwhile, the revival at the end of July, 1919, of a free market for gold, to which we shall refer below, provided an alternative method of remittance, and facilitated the return to more natural conditions than had been possible during the latter part of the war. From 18th September, 1919, drafts have been sold by open competitive tender, subject to a minimum rate and subject to the condition that no applicant may apply for more than 20 per cent. of the amount offered each week. The amount of drafts offered weekly is fixed on a consideration of the trade demand and the resources of the Government of India.

(b) RAISING OF RATE FOR SALE OF COUNCIL DRAFTS.

22. The rise in the price of silver to a point at which the bullion value of the rupee exceeded 1s. 4d. made the sale of Council Drafts at the rates fixed on 3rd January, 1917, impossible, except at a loss to Government. There was also a danger that if the rupee were undervalued it would tend to disappear from circulation, to be melted down and possibly to be exported. These tendencies probably existed in any case owing to the prohibition of the import of silver, but would have been aggravated by any undervaluing of the rupee. These considerations led to a series of changes in the rate of exchange. The first of these changes took place on 28th August, 1917, when the rate for immediate telegraphic transfers was raised from 1s. 4⅛d. to 1s. 5d. Shortly afterwards the Government of India announced that the price at which Council Drafts would be sold in future would be based roughly on the price at which silver could be bought, and this policy has governed alterations in the rate of exchange up to the present time. On 12th April, 1918, in consequence of the agreement with the United States Government for the purchase of silver from the dollar reserve at 101½ cents per fine ounce, the price for immediate telegraphic transfers was raised to 1s. 6d. This rate was maintained until 13th May, 1919, when the removal of the American control over the export of silver led to a rise in the price of the metal and necessitated a further rise to 1s. 8d. While we have been conducting our enquiries, the price of silver has broken all records, and the rate has been raised successively to 1s. 10d. on 12th August, 1919, to 2s. on 15th September, 1919, to 2s. 2d. on 22nd November, 1919, and to 2s. 4d. on 12th December, 1919. The last figure is now the minimum rate for the sale of immediate telegraphic transfers by competitive tender, while the Secretary of State has announced that he will sell reverse immediate telegraphic transfers at the rate of 2s. 3 29-32d. if the demand for them should arise. Thus the rate of exchange has been raised by successive steps from 1s. 4d. to 2s. 4d, as shown in the following table:—

Date of Introduction.	Minimum Rate for Immediate Telegraphic Transfers.
3rd January 1917	1 4⅛
28th August 1917	1 5
12th April 1918	1 6
13th May 1919	1 8
12th August 1919	1 10
15th September 1919	2 0
22nd November 1919	2 2
12th December 1919	2 4

(c) PURCHASE OF SILVER.

23. These modifications of system would not have been effectual in meeting the situation unless special measures had also been taken to increase the supply of currency. In February 1916 the necessity for rupee coinage on a large scale became apparent and the Secretary of State began to purchase silver. In 1915-16 and the subsequent years he bought in the market the amounts shown below. To facilitate his operations, by excluding from the market Indian buyers who would otherwise have bought for non-coinage purposes, the import of silver into India on private account was prohibited on the 3rd September 1917. This measure, however, removed only a few of the smaller competitors for the world's diminished supply of silver, and the world demand remained so heavy that it was impossible to satisfy India's demand without tapping sources of

supply outside the ordinary market. The Government of the United States of America, therefore, were approached, through His Majesty's Government, on the subject of releasing a portion of the silver dollars held in their reserve. These representations met with a ready response, and on 23rd April 1918 the United States Congress passed the Pittman Act, which authorised the sale to other Governments of silver not exceeding 350,000,000 silver dollars from the holding in the dollar reserve. Of this amount the Government of India acquired 200,000,000 fine ounces at 101½ cents. per fine ounce. Delivery in India began in July 1918, and was spread over a period of about a year. The timely help thus rendered by the United States Government in placing at India's disposal a supply of silver which represents considerably more than the world's annual mine production since 1914, enabled the Government of India to tide over a very serious currency crisis and to maintain the convertibility of the note issue.

The following table shows the amount of silver purchased by the Secretary of State in the last five years:—

	In open Market (Standard Ounces).	From United States Dollar Reserve (equivalent in Standard Ounces).
1915-16 ...	8,636,000	—
1916-17 ...	124,535,000	—
1917-18 ...	70,923,000	—
1918-19 ...	106,410,000	152,518,000
1919-20 (to 30th November 1919	14,108,000	60,875,000
Total ...	324,612,000	213,393,000

The total amount is thus 538,005,000 standard ounces.

(d) MEASURES FOR CONSERVATION AND ECONOMY OF SILVER.

PROHIBITION OF EXPORT AND MELTING.

24. These special measures for obtaining silver were supplemented by endeavours to protect the currency against depletion by export or melting. From 29th June, 1917, the use of silver or gold coin for other than currency purposes has been illegal, and from 3rd September 1917 the export of silver coin and bullion from India has been prohibited except under license. Steps were also taken to economise silver by the issue of Rs. 2½ and one-rupee notes, to which we shall refer in more detail below, and by extending the use of nickel for coin of small denominations. At the end of March 1918 a new two-anna nickel coin was issued to replace the silver two-anna piece, and this new coin has been so readily accepted that legislation was passed in September 1919 authorising the issue of four-anna and eight-anna nickel coins. The eight-anna nickel piece will not be unlimited legal tender like the corresponding silver coin; it will be legal tender up to one rupee only. We understand that the new coins will be issued at an early date.

(e) ACQUISITION AND USE OF GOLD.

25. In view of the shortage of silver it was important that the Government stock of gold should be as large as possible. With this object an Ordinance was issued on 29th June 1917, requiring all gold imported into India to be sold to Government at a price which, being based on the sterling exchange value of the rupee, took no account of the premium on gold as compared with sterling. The gold so obtained was placed in the Paper Currency Reserve as a backing against the issue of additional notes. To enable the gold bullion and foreign coin held by the Government of India to be converted into sovereigns without the delay involved by sending it to Australia for coinage and return, a branch of the Royal Mint was opened in Bombay in August 1918. Pending the establishment of the Royal Mint the gold mohur, a 15-rupee coin of the same weight and fineness as the sovereign, was minted as an emergency coin in order to supplement the stock of sovereigns available for issue as currency during the crisis of 1918. 2,110,000 gold mohurs and 1,295,000 sovereigns were coined in Bombay before the suspension of gold coinage in April 1919, when in view of difficulties in supplying the necessary staff it was decided to close temporarily the branch of the Royal Mint.

GOLD AS CURRENCY.

As we have mentioned above, the issue of sovereigns was stopped shortly after the outbreak of war. Owing to the demand for gold for social and industrial purposes and

the restricted supply, the bazaar price of the sovereign gradually rose and remained considerably above its statutory rate of Rs. 15. This premium on gold precluded its use as currency except in emergencies, but on two occasions attempts were made to prevent a further diminution of the rupee stocks by the issue of gold. At the beginning of 1917 gold bullion of the value of about £4,000,000 was sold and subsequently sovereigns to the amount of about £5,000,000, were issued for the purchase of crops in certain areas. Again, from February 1918, sovereigns and gold mohurs amounting to nearly £6,000,000 were issued for the financing of certain crops. The earlier issue of sovereigns was coincident with a large return of rupees from circulation, especially in those districts where sovereigns had been issued, but in 1918 the issue of gold was not followed by a return of rupees.

26. During the war the amount of gold which could be obtained by India was limited by the restrictions on its export from belligerent countries. The removal of the embargo on the export of gold by the United States Government on the 9th June 1919, and the freeing of the market for South African and Australian gold enabled India to obtain a larger supply. From 18th July 1919, immediate telegraphic transfers on India were offered against deposit at the Ottawa Mint of gold coin or bullion at a rate corresponding to the prevailing exchange rate. Very little gold was obtained from this source, and the arrangement was terminated on 15th September 1919. From 22nd August 1919 a limited amount of immediate telegraphic transfers on India were offered weekly for sale by competitive tender in New York, the proceeds of the sales being remitted to India in gold. Towards the end of October the demand for these transfers fell off and the sales were discontinued. The amount of gold obtained in this way was about 467,000* fine ounces. Arrangements were also made for the direct purchase of gold in London, the United States and Australia, and by 30th November 1919, about 2,485,000 fine ounces had been purchased. Finally, on 15th September 1919, the rate paid by the Government of India for the acquisition of gold brought into India on private account was fixed so as to include the premium on gold over sterling as measured by the dollar-sterling exchange, and has been varied from time to time approximately in accordance with the fluctuations of this exchange. The effect of the change in the basis of the acquisition rate was to re-establish an effective gold point, and to facilitate the import of gold in payment for export as an alternative to the purchase of Council Drafts. The amount of gold imported on private account and tendered to the Government of India between 15th September and 30th November was approximately 345,000 fine ounces.

27. In order to make a portion of the gold so obtained available for the use of the public of India, the Government of India announced, at the end of August 1919, that sales of gold would be held fortnightly until further notice, and that in each of the first three months not less than the equivalent of the gold content of 1,000,000 sovereigns would be offered for sale. The amount offered at the second sale in November was increased to 500,000 tolas (equivalent to nearly 800,000 sovereigns), and it was announced that this amount would be offered fortnightly for the three months beginning from December. The immediate effect of these sales was a considerable drop in the bazaar price of gold. The price of English bar gold fell from Rs. 32.12 per tola (Rs. 20.9 per sovereign) on 15th August to Rs. 27 per tola (Rs. 16.5 per sovereign) and 22nd September, but by the end of October the market had recovered and the price was Rs. 29.12 per tola (Rs. 18.11 per sovereign). At the beginning of December the price had again fallen to Rs. 28.5 per tola (Rs. 17.11 per sovereign). The total amount of gold sold up to 30th November amounted to about 2,159,000 tolas, being the equivalent of the gold content of about 3,439,000 sovereigns.

(f) INCREASE IN THE NOTE ISSUE.

EXPANSION OF NOTE CIRCULATION.

28. The difficulties of obtaining sufficient quantities of the precious metals for coinage purposes, and as backing for the issue of additional notes, made it necessary to increase the fiduciary portion of the note issue. Prior to the war the invested portion of the Paper Currency Reserve was limited by law to 14 crores of rupees. Since the beginning of November 1915, the legal limit of the invested portion of the Reserve has been modified nine times and now stands at 120 crores, of which 20 crores may be invested in securities of the Government of India. During this period the gross circulation of notes has increased nearly threefold, while the percentage of metallic backing has decreased by nearly one-half. The following table shows the growth of the circulation and the changes in the composition of the Reserve:—

Date.	Lakhs of Rupees.					Percentage of Total Metallic Reserve to gross Note Circulation.
	Gross Note Circulation.	Composition of Reserve.				
		Silver.	Gold.	Securities.	Total.	
31st March 1914	66,12	20,53	31,59	14,00	66,12	78·9
,, 1915	61,63	32,34	15,29	14,00	61,63	77·3
,, 1916	67,73	23,67	24,16	20,00	67,73	70·5
,, 1917	86,38	19,32	18,67	48,49	86,38	43·9
,, 1918	99,79	10,79	27,52	61,43	9 ,79	38·4
,, 1919	153,46	37,39	17,49	98,68	153, 6	35·8
30th November 1919	179,67	47,44	32,70	99,53	179,67	44·6

The use of paper currency was further stimulated by the issue in December 1917 and January 1918 of notes for Rs. 2½ and one rupee respectively, to supplement the notes of Rs. 5 and higher denominations already in circulation. At first these notes of small denomination did not circulate to any appreciable extent, but later, when the supply of rupees was curtailed, their circulation increased rapidly, and on 31st March 1919 the gross circulation exceeded Rs. 1,84 lakhs in the case of the Rs. 2½ denomination and Rs. 10,50 lakhs in the case of the one-rupee denomination.

RESTRICTIONS ON ENCASHMENT.

29. The encouragement of the use of notes by the provision of ample facilities for their encashment had been one of the most prominent features of the currency policy of the Government of India in the years preceding the outbreak of war, and this policy was continued as long as the supply of rupees was adequate. From 1916, owing to the causes which we have already indicated, the absorption of rupees was abnormally large, the figure for 1916-17 being Rs. 38,81 lakhs and for 1917-18 Rs. 27,86 lakhs; and on 1st April 1918, the silver balances had fallen to under 10½ crores, or about 8 crores less than what was considered a safe minimum in the period before the war. The unfavourable war news in March and April 1918 caused a run on the Bombay Currency Office for the encashment of notes, and this was followed by similar difficulties elsewhere, notably in Lahore. Inconvertibility appeared to be inevitable, and was only averted by the energy and resource of the officers responsible, and by the timely announcement of the acquisition of the Pittman silver. By the first week in June the rupee balance had diminished to little more than 4 crores. From July the delivery of the Pittman silver commenced and the situation gradually improved, but the necessity for conserving their reduced stock of rupees had forced on the Government a reversal of their previous policy. Facilities for the encashment of notes at district Treasuries were in a large degree withdrawn. The conveyance of specie by rail and river steamer was prohibited, and an embargo was placed on its transmission by post. Later, in January 1919, owing to the practical administrative difficulties of dealing in full with the demands for encashment at the Currency Offices during the busy season, the daily issues of rupees to single tenderers of notes were limited to a figure which made it practicable to satisfy large demands in part and small demands as a rule in full. The result of these restrictions was the substitution to a large extent of notes for rupees as the common circulating medium.

The evidence which we have had regarding the extent of this substitution, and the ease with which it was accomplished, is rather indefinite. The continued abnormal absorption of rupees—Rs. 45,02 lakhs were absorbed in 1918-19—points to a very large use of rupees as currency. On the other hand, there is little doubt that large quantities of rupees have been retained as a store of value or have been used for industrial purposes in spite of the prohibition of melting, while the purchase of jute,

cotton and other crops from the cultivators has recently been effected almost entirely by means of notes. There was in many parts of India a considerable discount on notes, especially the new Rs. 2½ and one-rupee notes, when they were first issued in large quantities to replace rupees. Discounts as high as 15 per cent. and 19 per cent. have been reported; but the discount rapidly diminished when it was seen that the notes were freely accepted in payment of Government dues and when small coin was made available in large quantities. The reports received by the Government of India in the year 1919 do not show any discount on the notes as compared with silver coin exceeding 3 per cent.

FINANCIAL MEASURES.

30. Our summary would be incomplete without a brief reference to other financial measures which affected the currency situation indirectly. Throughout the war ordinary expenditure and, in particular, capital expenditure, were kept as low as possible, while from 1916-17 onwards additional taxation was imposed which, together with the normal growth of revenue, raised the total revenue of the Government of India from £84,413,500 in 1915-16 to an estimated figure of £123,404,200 for 1919-20. The resources available for meeting the heavy war expenditure in India were further increased by extensive borrowing in India. The loans of 1917, 1918 and 1919 yielded about Rs. 130 crores and from October 1917 short-term Treasury Bills have been issued in considerable quantities, the amount outstanding on 30th November 1919, being about Rs. 65.58 crores.

These measures materially assisted towards meeting the heavy demand for remittance to India.

SUMMARY OF PRESENT POSITION.

31. We may now summarise the main facts of the present position. Council Drafts are being sold by competitive tender, subject to a minimum rate, at present 2s. 4d. sterling, the amount being fixed weekly by the Secretary of State. It has been announced that reverse immediate telegraphic transfers will be sold at the rate of 2s. 3 29-32d. if the demand for them should arise. All gold imported into India has to be sold to Government at a prescribed price. The rate fixed contains an allowance to cover the premium on gold over sterling. As there is now a free market for gold, this import acquisition rate, which is varied from time to time in accordance with the movement of the dollar-sterling exchange, fixes an upper gold point which tends to prevent the rate bid for Council Drafts from rising above the minimum rate by much more than the cost of shipping gold, except possibly for short periods when the demand for remittance is urgent. The rate in force for the sale of Reverse Councils fixes a limit to the fall of exchange so long as the means for meeting them are available.

The sovereign is still legal tender in India for Rs. 15, and the Government is under an obligation to pay Rs. 15 for sovereigns presented for encashment. As, however, the bazaar price of gold is considerably above this parity, sovereigns have disappeared from circulation and are not being issued by Government. The import and export of silver are prohibited, and its price is at a level which prevents purchases by the Secretary of State for coinage except at a loss. The restrictions on the encashment of notes to which we have referred in paragraph 29 are still in force.

32. We have now completed our sketch of the developments in the Indian exchange and currency system since 1914. Before passing on from this section of our Report, those of us who are not connected with Indian official administration desire to place on record our recognition of the skill, courage and resource which the Government of India and the authorities at the India Office have shown in dealing with the complicated and ever-changing problems that presented themselves throughout the latter part of the war in connection with the Indian currency system.

Conclusions and Recommendations.

INTRODUCTORY.

33. Having traced the history of the Indian currency system during the period of the war we proceed to state the conclusions which we draw from it, and our recommendations for future action.

The system built up since 1893 worked well, and was beneficial to India. It supplied suitable media for the internal circulation, provided means for the settlement of the balance of trade, and secured stability between the rupee and sterling, which until recently was in practice synonymous with gold. It has proved effectual in preventing the fall in value of the rupee below 1s. 4d. and unless there should be profound modifications in India's position as an exporting

country with a favourable trade balance, there was no reason to apprehend any breakdown in this respect.

But the system was not proof against a great rise in the value of silver. In framing it this contingency had not been taken into account. So little was it anticipated, that the system was not criticised on this ground, so far as we are aware, by any of the witnesses who have appeared before the successive Committees and Commissions on Indian currency. But the unexpected has happened. The price of silver has risen to unprecedented heights, partly, as we have seen, owing to the shortage of supplies from Mexico (caused by internal conditions independent of the war), and partly owing to causes arising out of the war, with the result that there has been extreme difficulty in obtaining the silver required for Indian currency, that the convertibility of the note issue has been in danger, and that the exchange value of the rupee has been raised by successive steps from 1s. 4d. to 2s. 4d.

STABILITY OF EXCHANGE.

34. The terms of our reference place before us as one of the objects of our enquiry the re-establishment of stability. We find it necessary, before formulating our recommendations, to examine in what respects exchange stability is important, and what degree of urgency attaches to its re-establishment.

The evidence we have received was unanimous as to the benefit which India has derived from the maintenance of a fixed rate of 1s. 4d. per rupee for the 20 years from 1898 to 1917; but some witnesses expressed the opinion that fixity is not indispensable. Our conclusion, after considering the views put before us, is that, for the current operations of trade, stability is an important facility rather than an essential condition. There are many instances, including that of India herself before the closing of mints, which show that trade has flourished, and can flourish, with a fluctuating exchange. The conditions are somewhat more speculative, but the difficulties which may arise are not insuperable, and the banks are not slow to supply machinery which enables the merchant to cover his risks.

This is specially true of day-to-day fluctuations of exchange of moderate scope, if the movements are of greater extent and produce large changes in the basis of relative values, a different set of considerations comes into play. For a time, at any rate, a large rise in exchange tends to stimulate the import trade and to impede the export trade, while the reverse effect is produced by a fall in exchange. If exchange is made stable at a new level we believe that these effects are in the main transitory, and do not continue beyond the period necessary for wages and other elements of cost to adjust themselves to the new conditions. But this process of adjustment is a difficult and sometimes a prolonged one, and causes severe strains in the social fabric.

35. The question must also be considered in relation to the movements of capital. Stability is a necessary condition for the free investment of external capital in India as well as for the protection of capital already invested. The effect on new investments may be less important in the next few years, since it is to be anticipated that Indian capital will play an increasing part in the development of Indian resources, and that owing to the urgent demands arising in the United Kingdom and elsewhere, the supply of external capital available for India may be comparatively small. The above observations apply specially to permanent or long-term investment; but they are also true as regards the more liquid employment of money. A stable exchange facilitates the free movement of funds to and from India, thus assisting commercial finance and tending to avert temporary stringencies.

OBJECTIONS TO INSTABILITY.

Whatever the evils and inconveniences of instability may be, they are increased if the movements of exchange are brought about not by the automatic action of economic causes, but by administrative acts. The commercial community are prepared to deal with fluctuations in exchange as well as with fluctuations in the other elements entering into a transaction, and to provide against any risks that may arise; but they feel that if official action intervenes to interpret the play of natural forces and to give effect to them, an element of uncertainty is introduced which is beyond their reckoning. However complete the integrity and however great the intelligence on which official action is based, an automatic system, which does not depend upon such action for its operation, is greatly to be preferred.

36. Our conclusion, therefore, is that a stable level of exchange gives the most healthy condition for production and trade, and for the employment of capital, and that large changes in the exchange value of a currency are an evil, which should be avoided so far as possible; but if a large change has taken place it may be preferable to establish stability at the new level rather

than to submit to the further change which is necessary for a return to the old level, especially if the former course shortens the periods of uncertainty.

The object should therefore be to restore stability to the rupee at as early a date as practicable, and also to restore the automatic working that characterised the Indian currency system in the past.

Modifications of System.

37. It will be convenient to consider, first, certain special proposals that aim at giving stability to the exchange value of the rupee in such a way as to avoid the necessity for following the price of silver to higher levels, or, in the view of some witnesses, with the object of making it possible to revert to a value for the rupee not much above the old level of 1s. 4d. In a later part of this Report (paras. 44-54) we give our reasons for considering a high exchange value to be preferable to a low value; but as the proposals to which we refer are inadmissible on other grounds, it is desirable to deal with them at the outset.

(i) REDUCTION OF THE FINENESS OR WEIGHT OF THE RUPEE.

38. It has been suggested that a new rupee should be issued having a lower silver content than the present coin. If the existing standard of fineness or the weight were sufficiently reduced, it would be possible to fix the exchange value of the rupee at any level that might be chosen, and to maintain its token character however great the rise in the price of silver might be.

The evidence we have taken was decisively hostile to this proposal. It has been urged in support of it that in the Straits Settlements and elsewhere the reduction of the silver content of full legal tender coins has been successfully made; but in none of the cases brought to our notice were the conditions similar to those existing in India. The fineness of the present rupee, which is known to every village goldsmith and silversmith, has remained unaltered since 1835, and its use is so firmly rooted in the habits of the Indian people as to have given it the character of a standard weight. Modification of the fineness or weight of the standard coin of the country would, we have been assured, react gravely on the credit of the Government, and possibly lead to serious social and economic consequences. A new rupee of lower silver content would, in accordance with Gresham's law, tend to drive the present rupee out of circulation, and very large quantities of the new rupees would be required to meet demands for metallic currency. Even if the problem of minting on the scale required could be overcome, there might be great difficulty in obtaining the necessary supplies of silver either from existing currency or otherwise. We concur, therefore, in the view of the Government of India that proposals of this character must be dismissed as impracticable.

(ii) ISSUE OF 2 OR 3-RUPEE COINS OF LOWER PROPORTIONAL SILVER CONTENT.

39. A suggestion of a similar nature is that while the shortage of silver continues, 2 or 3 rupee pieces of lower proportional silver content than the rupee should be issued, with the intention that they should circulate side by side with the existing rupee, the coinage of which would be temporarily suspended. This proposal is open to many of the objections stated in the previous paragraph. Rupees would tend to disappear from circulation before the competition of the new and baser coins, and the credit of the Government would be affected by the decision to stop the minting of the coin to which India has been so long accustomed. Moreover, a 2 or 3-rupee unit would be inconveniently large for the great bulk of retail transactions in India.

(iii) NICKEL COINS.

40. For the same reasons we are unable to support the suggestion that a nickel rupee should be issued, either alone or in association with 2 or 3-rupee pieces of lower proportional silver content than the existing rupee; but we welcome the recent legislation of the Government of India authorising the issue of 4-anna and 8-anna nickel coins. Witnesses who have appeared before us have emphasised the fact that the reluctance to use Rs. 2½ and one-rupee notes when these were first issued in large quantities was due in great measure to the difficulty of obtaining small change. We hope that abundant supplies of the new nickel coins will be made available as soon as possible, and if the low legal tender limit of one rupee for the 8-anna nickel piece should prove an obstacle to its free circulation the question of raising the limit to Rs. 5 or Rs. 10 should be considered.

(iv) INCONVERTIBLE NOTE ISSUE.

41. Another proposal aiming at the establishment and maintenance of a stable exchange, even though silver should continue to rise in price, is that which was put forward by the Government of India before our enquiry began. Circumstances have changed since then, especially by the establishment

of a free gold market, and the later proposals of the Government of India are of a different character; but it is necessary to explain the reasons against the adoption of the earlier proposal.

It was proposed that exchange should be stabilised at a rate which could reasonably be expected to afford an assurance that the rupee would remain a token coin. If, contrary to expectations, the price of silver should rise to a height which would defeat this assurance, the Secretary of State should be prepared to suspend the purchase of silver. In that case it would probably be impossible to provide silver coin to meet the demands of India, and the notes would become inconvertible.

It was suggested that this situation would not last long, since the Indian demand for silver is so important a factor in the silver market that the abstention of the Government of India from purchases would very soon bring about a fall in price. Recent experience, however, has shown that this result is not necessarily produced in all circumstances. For the last six months the Secretary of State has made no purchases of silver, but in spite of his abstention the price has risen to an unprecedented height. We cannot shut our eyes to the possibility that under the influence of an intense demand from China (such as has prevailed recently) or from some other quarter, a considerable period might elapse in which the price of silver might remain beyond the reach of the Government of India.

It was suggested also that the inconvertibility might be partial; that is to say, that the Government of India should take powers to restrict the issue of rupees from the Currency Offices and should issue them only under such conditions as they might think advisable. Some of the practical inconveniences of complete inconvertibility might be avoided in this way, but there would be difficulties in the administration of such a system, and we do not think that in its effect on the credit of the Government and on popular confidence in the note issue it would differ greatly from complete inconvertibility.

The evidence submitted to us was strongly opposed to allowing the note issue in India to become inconvertible, whether wholly or partially, if it can possibly be avoided. It is true that as a result of the war the paper currency has become practically, if not legally, inconvertible in many countries, including the United Kingdom. In Egypt, for instance, where the currency position was affected by influences in some respects similar to those that operated in India, the note issue has been inconvertible since August 1914, and the change was accomplished without difficulty. We believe, however, that the note-using habit is not yet sufficiently established in India to render the introduction of a similar measure there possible without grave risks. Until recently the circulation of notes outside the larger towns was comparatively small, and only two years have passed since notes of small denomination have been introduced. In many parts of the country the climate is not suitable for the use of paper money, and the preference for coin will probably prevail among the mass of the population for many years. In these circumstances a failure to maintain convertibility may be expected to lead to a considerable discount on the note, the extent of which cannot be predicted with any accuracy. The credit of the Government would suffer a severe blow, and if belief in the convertibility of the note were once shaken it might take many years of anxious labour to restore confidence, while the set-back to the development of a sound and economical monetary circulation in India would be disastrous.

We hold, therefore, that the maintenance of the convertibility of the note issue is a vital part of the Indian currency system.

Price of Silver.

42. We have in paragraphs 15-19 traced the causes of the rise in the price of silver. The enquiry conducted by Professors Cullis and Carpenter suggests that on the restoration of order in Mexico the pre-war figures of production will again be reached, and that it is possible that the increasing world demand for the base metals with which silver is associated as a by-product, together with improvements in the method of extraction and the stimulus of high prices, may at an early date lead to a considerable increase in production. On the other hand, the evidence suggests that the demand for silver is likely to continue for a few years on a large scale. The general rise in prices creates a demand for increased supplies of subsidiary silver coinage throughout the world, and though the high price of silver may tend to reduce the demand for the arts, it is difficult to say whether the reduction will be on a sufficient scale to influence appreciably the price of the metal. We have been unable to obtain any reliable evidence regarding the probable demand from China in the near future. As we have stated, China has already imported sufficient silver to counterbalance her exports during the war, but she is still buy-

ing, and it is impossible to foresee how long her demand is likely to continue. It would be rash, therefore, to formulate any definite conclusion as to the level at which the price of silver is likely to stand.

43. There are, however, certain considerations which must be taken into account. The Pittman Act imposes on the United States Government the obligation of replacing the silver taken from their reserves, and lays down that until this silver has been replaced they must buy for this purpose at the price of one dollar per fine ounce any silver "of the product of mines situated in the United States, and of reduction works so located" which is tendered to them for purchase. As this replacement will involve the acquisition of considerably more than a year's total production of silver on the present basis of output, while the world's demand for silver is likely to remain high, the process of replacement cannot be completed for some years. During the interval the price of silver cannot be expected to fall below one dollar per fine ounce. Even when the dollar-sterling exchange returns to par, it will be impossible to mint rupees without loss from silver purchased at this price unless the exchange value of the rupee is fixed at 1s. 6d. or some higher figure.

It is more difficult to form any conclusion as to the maximum beyond which the price of silver is unlikely to rise. When the exchanges are at par, the prices of silver at which the principal silver coinages of the more important countries have a bullion value equivalent to their nominal value, are as follows:—England, 66d.; France (5 franc piece), 60¾d.; U. S. A. (dollar), 59¼d. If the price of silver were to remain for any long period at a level substantially over that corresponding to the above figures, it would threaten the silver coinages of France and the United States with the risk of depletion by melting and export and would also offer inducements to these countries to convert their silver reserves into gold at a favourable rate. In support of this view, we may refer to the recent announcement that the American Treasury has decided to sell to certain American Banks established in the Far East silver obtained by melting the available dollars in their possession (now $55,000,000) at their gold equivalent of 129·29 cents., plus melting, insurance, and shipping charges, whenever that price can be obtained, the intention, presumably, being to prevent silver rising to a point which would lead to the melting down of subsidiary coin. When the price of silver is 137·8 cents per fine ounce, corresponding to 62.9d. (gold) per standard ounce, and therefore well above both the French and the American parity, the corresponding bullion value of the silver in the rupee is 1s. 11.36d. (gold), and the cost of the rupee (including all charges) is approximately 2s. (gold). We believe that, if the exchange value of the rupee is fixed at a figure not lower than this, there is substantial ground for holding that the rupee can be established as a token coin, and the maintenance of a satisfactory monetary circulation in India assured.

Effects of High Exchange.

44. Our conclusion that a high level of exchange is essential for the establishment of a sound monetary system leads us to a consideration of the more general economic effects of a high rate. Some of the witnesses who have appeared before us have laid great stress on the dangers attending a high level of prices in India, and on the beneficial effect of a high rate of exchange in restraining the rise of prices; others have expressed apprehension as to the effect that a high rate of exchange might have on the well-being of the people of India, the maintenance of Indian trade and the development of Indian industry. We recognise the great importance of the arguments laid before us from these opposite points of view, both in oral evidence and written memoranda, and we now proceed to examine the issues raised by this aspect of the case. This review will lead us to consider the effect of a high rate of exchange on the remittance of funds from India to meet the requirements of the Government.

(a) EFFECT ON THE LEVEL OF PRICES IN INDIA.

45. At the outset of our enquiry we requested the Government of India to furnish us with up-to-date information regarding price movements in India. The particulars we received in response to our request will be found on pages 159 to 176 in the volume of Appendices to our Report, and we invite attention to the memorandum submitted by the Government of India on the subject.

In illustration of the rise in the price of necessaries of life we cite the following index numbers for the prices of selected articles in 1914, 1915-17, and 1918-19, based on the average wholesale prices for 1900-09

which are taken as the equivalent of 100.

	1914	1915-17.	1918-19
Wheat ...	118	135	180
Country rice ...	126	122	139
Ghi ...	132	136	183
Jawar ...	123	103	236
Bajra ...	130	123	249
Dal ...	125	130	166
Raw sugar (gur) ...	101	134	148
Country salt ...	111	214	413
Cotton piece goods (Indian made)	109	94	164
Cotton piece goods imported).	112	138	206

The following table exhibits the rise in Indian prices since 1910, this year being taken as the basic year for the preparation of the table :—

Index Numbers of Prices in India.

Year	Special Idex Number for Food Grains (Retail Prices). Col. 1.	Special Index Number for imported Articles (Wholesale Prices) Col. 2.	Special Index Number for Articles exported (mostly Wholesale prices). Col.3.	General Index Number for the Articles covered by Columns 2 and 3. Col 4.
1910 ...	100	100	100	100
1911 ...	96	104	107	106
1912 ...	112	107	114	112
1913 ...	118	107	121	117
1914 ...	132	105	126	120
1915 ...	120	134	122	125
1916 ...	120	217	128	151
1917 ...	120	240	134	161
1918 ...	161	265	157	184

For comparison with the above we give for the same years corresponding figures deduced from Mr. Sauerbeck's tables for prices in the United Kingdom, which, though based entirely on wholesale prices, may serve to give an indication of the comparative rise in the two countries :—

Year.	Index Nos. of Prices in United Kingdom.	General Index Nos. for the Articles covered by Cols. 2 & 3 (see Col. 4 above)
1910	100	100
1911	103	106
1912	110	112
1913	110	117
1914	110	120
1915	139	125
1916	176	151
1917	226	161
1918	249	184

46. It will be seen from these tables, and from the more detailed information contained in Appendix XXVIII, that there has been a great increase in all prices in India in the last few years. The upward movement had begun before the war, but it has continued, and during the last two years its rapidity has greatly increased. The serious and widespread failure of crops in 1918 was in part responsible for the special rise in the price of food grains in 1918-19; but the general upward movement is mainly due to causes resulting from the war, including the excessive creation of credit and paper currency and restraints upon free commercial intercourse, which have raised prices throughout the world and have been operative in India as well as elsewhere.

The figures show that on the whole the rise of prices in India has not been so great as the rise in the United Kingdom. A similar conclusion would probably be reached if a comparison were made between Indian prices and prices in other countries outside India whose currencies are depreciated. Amongst the various causes, not easily to be disentangled, which have contributed to this result, the one which specially concerns us is the rise in the exchange rate of the rupee. We shall examine later the operation of this cause and the inferences to be drawn from it as to the level of exchange which it is desirable to establish; but in the first place we proceed to examine the economic effects of a rise in prices on the population of India.

EFFECT OF RISE IN PRICES.

47. As India is a country whose export trade is more valuable than her import trade it might be thought that an increase in prices would be on the whole advantageous to her. This view has been strongly

represented by some of our witnesses; whilst others have expressed equally strongly the opinion that any considerable increase in prices is an evil and a danger. In order to decide between these conflicting views, we have endeavoured to examine the effect of rising prices on the main classes of the population.

According to the census of 1911, 217 millions, that is, 72 per cent. of the population of India, are engaged in pasture and agriculture. But this number embraces classes who are differently affected by the rise in prices. Of 167 million cultivators of their own or rented land, those who have a surplus for sale would ordinarily benefit by a rise in the price of the commodities they produce, but even these—and perhaps their position is the most favourable—have had to contend with the large increase in the price of imported articles, notably cotton piece goods and other necessaries of life. Moreover, if, as is often the case, the cultivator has received advances for his maintenance and for seed, repayable in grain after the harvest, any increase in the value of the grain repaid benefits the money-lender and not the cultivator. On the other hand, the agriculturist who has little surplus produce to sell and lives on what he produces, would, in so far as he maintains himself on his own produce, be unaffected by a rise in the price of foodstuffs, and he would have only a small profit to set against the heavy rise in the cost of the articles he has to buy. The numerous class of farm servants and field labourers, estimated in the census of 1911 at over 41 millions, would ordinarily stand to lose by a rise in prices, except in so far as their wages are payable in kind and not in money. The large class of persons with fixed incomes, which would include persons living on rents, Government servants, professional men, and pensioners, have suffered severely from the rise in prices of the commodities they require, and the urban population, who are not producers, may be placed in the same category. Industrial wage-earners, labourers, and domestic servants have, as a result of increased demands for their services during the war, been able to obtain increased wages. But the evidence which we have received suggests that wages generally in India have advanced more slowly than prices, and much suffering is entailed in the course of the adjustment of wages to new price levels.

VIEW OF GOVERNMENT.

48. The general effect of the rise in prices is summarised in the following passage, which we quote from the Government of India's memorandum:—

"The effect has of course been felt most directly by the poorer classes, but it has reacted on all sections of the community. Complaints on the subject have been universal throughout the country, and it is reported from the districts that in recent months the topic of high prices has engaged the minds of the people at large to the exclusion of every other; they could understand dearness during the war, but cannot understand why prices do not fall now that the war is over; they can account for some of the rise in the price of food-grains by last year's poor monsoon, but they are puzzled by large increases in the prices of their other necessities of life, the supply of which is not dependent on a good rainfall. There is no longer any room for doubt that the resultant increase in the expense of living due to the high prices of food-grains, as also of other necessaries, such as cloth, kerosene oil, and the hardships which this increase has entailed on the poorer classes and those on fixed incomes, have been a very important factor in promoting unrest and discontent. At the same time the cultivator, who would ordinarily be the first to profit by the high prices of produce, whether food-grains or other raw material such as jute and cotton, has seen his profits disappear owing to the simultaneous rise in the price of other necessities. The wages of manual labour have no doubt been to some extent readjusted, and ultimately the wages of the clerical and other classes of employees will undergo a similar readjustment. But the process of adjustment, however rapid, must inevitably be a painful one, which no amount of administrative palliatives, such as control of distribution, can alleviate."

These views are not a matter of theory alone. Disturbances have actually arisen in various parts of the country from time to time as a result of high prices, and the social and economic discontent to which they give rise is especially serious in a country where the mass of the population is ignorant and uneducated, and inclined to attribute all calamities to the action of the Government. The rise in prices in India has now reached a point at which it is injurious to the country as a whole, and we believe that any measures tending either to reduce prices or to check a further increase would be beneficial to the mass of the population.

49. The exceptional conditions under which trade was conducted in the course of the war make it impossible to arrive at any precise conclusions as to the extent to which the rise in prices has been influenced by the

rise in the exchange value of the rupee. Government control over the movement and prices of food-grains in India undoubtedly prevented prices rising to the full extent that might otherwise have been the case. Restrictions on finance and freight also exerted a powerful influence in the same direction. Again, the scarcity in 1918 operated to raise the prices of food-grains to an abnormal height. While these complicated factors make it impossible to estimate in precise terms the effect of the rise in the exchange value of the rupee on Indian prices, we see no reason to doubt that, in accordance with accepted economic theory, Indian prices would, but for the rise in exchange, have been still further enhanced. Taking the case of imported commodities, the sterling price at which the merchant can lay down goods in India is determined by the cost of production and the transport and other charges. If the exchange value of the rupee rises, this sterling cost is represented by a smaller number of rupees, and the goods can be sold at a lower rupee price. Again, in the case of exports such as wheat, whose price outside India is determined by world-wide conditions of production and consumption, the sterling price which can be obtained for a given quantity of wheat will, if exchange rises, be represented by a smaller number of rupees, and the price which the grower will receive must necessarily be lower.

These considerations do not apply with equal force to exported produce such as jute, of which India enjoys a practical monopoly, since, if exchange rises, the Indian producer has it in his power to exact a larger sterling price in order that he may receive the same number of rupees. But even for such commodities as jute, the power of varying the price to be paid by the consumer is far from absolute, and it is probable that a higher exchange means a somewhat lower price to the producer. Nor do precisely the same considerations apply to products which are grown almost entirely for internal consumption, as, for instance, food-grains such as jawar or bajra. While, however, movements of exchange have little direct effect on the price of such products, it is probable that they have indirect effects which give a result similar in kind though less in degree.

50. We are led therefore to the conclusion that on economic and social grounds it is not desirable to restore a low level of exchange for the rupee under present conditions. Such a level would tend to augment prices generally and to aggravate the dangers of social and economic discontent. Having regard to the conditions under which the large mass of the population lives, we are satisfied that in so far as the rise in exchange has mitigated a rise in Indian prices, it has been to the advantage of the country as a whole, and that it is desirable to secure the continuance of this benefit.

(b) EFFECT ON INDIAN TRADE.

51. We now pass on to consider how far Indian commerce is likely to be affected by the maintenance of the exchange value of the rupee at a high level. We have already referred to the effects of a rise in exchange in stimulating imports and checking exports, and have expressed the opinion that these effects are transitory, and that they are no longer operative when wages and other elements of cost have adapted themselves to the new level of exchange.*

Indian trade is at present prosperous, and India is in a favourable position for maintaining this prosperity. The world shortage of raw materials and foodstuffs is likely to ensure a continuing demand for Indian produce during the period necessary for complete adjustment, while the great rise in the level of prices in countries importing from India should generally enable the Indian producer to obtain a satisfactory rupee price for his commodities in spite of the high exchange. It has, moreover, to be remembered that a high exchange brings with it certain counter-balancing advantages even to producing interests. It tends, for instance, to keep down the cost of imported stores and machinery as measured in rupees, and, as we have pointed out above, exercises a check on the rising cost of living in India and consequently on the rise in wages.

We do not think it necessary to enter into a detailed review of the conditions under which trade in India's staple products is conducted. Some of these commodities, of which jute is the most important, are virtually monopolies with assured markets, while others, such as tea, cotton, seeds and hides, are articles for which the world demand is insistent despite the high range of prices. Exchange is only one and not necessarily the most important factor of which account has to be taken. After careful consideration of the evidence placed before us we have arrived at the conclusion that Indian trade is not likely to suffer any permanent injury from the fixing of exchange at a high level.

*This question was discussed fully in the Report of the Herschell Committee of 1893 (paras 27 and 116-120). See also Memorandum received from the Government of India regarding Indian price movements (Appendices p. 164, § 15).

There is one qualification which it is necessary to add to the above statement. It seems probable that prices generally will remain at a high level for a considerable time, and that any return to lower level will be gradual; but if, contrary to this expectation, a great and rapid fall in world prices were to take place, a new element of disturbance would be introduced. The costs of production in India might fail to adjust themselves with equal rapidity to the lower level of prices, and Indian exports might suffer to an extent which would endanger the maintenance of exchange at the level which we propose. In that case it would be necessary to consider the problem afresh, and take the measures which might be required by the altered circumstances.

(c) EFFECT ON INDIAN INDUSTRIAL DEVELOPMENT.

52. Our attention has been drawn by certain witnesses to the important movement that is now taking place in the development of industry in India, and some apprehension has been expressed lest a high rate of exchange should exercise a retarding influence on this welcome activity. We recognise that competitive imports into India may be temporarily stimulated by the high rate of exchange, especially from countries where the cost of production is low; but even in the period which may elapse before the adjustment of prices and other conditions to the new level is complete, this influence, so far as manufactured articles from Europe and America are concerned, is likely to be counteracted by the greatly increased cost of production in the exporting countries at the present time. Moreover, a high exchange will tend to retain for India the advantage of a low cost for wages and raw materials, and in so far as nascent industries are dependent on imported machinery, plant and stores, they will benefit from the lower rupee prices payable for them. On a review of all the facts, we are of opinion that the development of Indian industry will not be seriously hampered by a high rate of exchange.

(d) EFFECT ON HOME CHARGES.

53. One of the reasons for the closing of the mints to the free coinage of silver in 1893 was the increasing difficulty experienced by the Government of India in providing for their sterling obligations when the exchange value of the rupee was continuously falling. The fixing of the rupee at 1s. 4d. materially improved the revenue position and enabled the Indian Treasury to do without the additional taxation that would otherwise have been necessary. A high rate of exchange would result in further advantages in this direction. When the exchange value of the rupee was 1s. 4d. the rupee equivalent of the Home charges on the basis of £25,000,000 a year was 37½ crores; while, if the necessary sum were remitted at an exchange of 2s., the cost would be 25 crores only, a saving of 12½ crores.

On the other hand there would be a loss involved in the revaluation in rupees of the sterling investments and the gold in the Paper Currency Reserve.

If the revaluation were made at 2s. to the rupee, the depreciation to be made good would amount to 38.4 crores. If the whole of the revenue saved in respect of the Home charges could be employed for the purpose of meeting this loss it would be recouped in about three years. Thereafter a considerable surplus revenue would remain which might be employed in furthering the development of India or in the reduction of taxation.

This is an incidental advantage in fixing a high rate of exchange which must be taken into consideration.

54. We are thus led to the conclusion that the material interests of India are not likely to suffer from the fixing of a high rate of exchange for the rupee, and that certain important advantages will follow from such a course of action. The question now arises as to the manner in which the exchange should be fixed.

Gold or Sterling.

55. Before the war the convertibility of sterling into gold was complete. Sovereigns and half-sovereigns were in circulation, and Bank of England notes and other bank notes which were in use in the United Kingdom could be exchanged without any difficulty for gold. It was therefore unnecessary in considering the problems of Indian exchange to make any distinction between the two. At the present time, however, gold coin is no longer in circulation in the United Kingdom, and Treasury notes, which form the great bulk of the full legal tender currency, are not in practice convertible into gold. The result is that there is a divergence between the value of the pound sterling and the sovereign. One hundred ounces of fine gold can be coined into 425 sovereigns; but at the quotation on 17th December (108s. 9d. per oz.) 100 ounces of fine gold cost approximately £544 in sterling, i.e., in notes. Thus £1 sterling (paper) is equivalent to 425/544 or .78 of the sovereign (gold), a discount of 22 per cent.; or, conversely, the

sovereign (gold) is worth £544/425 or £1.28 sterling (paper), a premium of 28 per cent.

A corresponding depreciation is shown in the exchange between sterling and the American dollar, which is convertible into gold. The gold sovereign is equivalent to $4.8666, while the pound sterling was quoted on 17th December at $3,83, a depreciation of over 21 per cent.

It therefore becomes necessary to consider whether, if the rupee is to be stabilised, its fixed relation should be with sterling, as hitherto, or with gold. In the latter case the necessary result will be that, until the gold basis of the British currency is restored and sterling becomes equivalent to gold again, the rupee-sterling exchange will fluctuate in the same manner as the dollar-sterling exchange. This issue was brought into prominence by Mr. Lucas, Financial Secretary at the India Office, who in his written memoranda and oral evidence has argued the case for a fixed relation with gold with much force and ability. We have given anxious consideration to this question, and our unanimous conclusion is that, for the reasons which we proceed to state, the balance of advantage lies in fixing the relation of the rupee with gold rather than with sterling.

ADVANTAGES OF STERLING.

56. The main inducement for retaining the fixed relation with sterling is that a larger part of the trade of India is with sterling-using countries than with countries upon an effective gold basis. The only important countries to be placed at present in the latter class are the United States and probably Japan. The exports to these two countries in 1918-19 amounted to 25 per cent. of the total exports of India (as compared with 14 per cent. before the war), while the import trade from them was 30 per cent. of the total (as compared with 5 per cent. before the war). On the other hand, the trade with the British Empire (excluding those portions which do not use sterling) amounted to 40 per cent. for exports and 48 per cent. for imports. It is argued that the advantage of fixity of exchange should be retained for the most important section of India's trade; and also that, in the interests of the Empire as a whole, it is desirable that the exchange system should be such as to facilitate and promote trade within the Empire rather than outside it, and, we may add, to retain for centres within the British Empire the finance of Indian trade.

This consideration has undoubtedly some weight, especially as the effect of war conditions has already been to divert to Japan and the United States a part of the trade formerly exchanged with the United Kingdom and other European countries. We do not, however, consider that a fluctuating sterling exchange will create an obstacle of a serious character to trade between the United Kingdom and India or to existing methods of financing that trade, provided that the system in force is such as to enable trade requirements for remittance to be met readily and to their full amount. In any case the fluctuations of the rupee-sterling exchange will only exist until the gold basis of the British currency is restored.

ADVANTAGES OF GOLD.

57. The advantages, on the other hand, of fixing the exchange value of the rupee in relation to gold may be stated as follows:—

(i) Great and admitted inconveniences attach to a currency which is depreciated and may suffer further depreciation. If India's currency is linked to sterling it will share those inconveniences. Her position as an exporting country with a favourable trade balance enables her to avoid them by linking her currency to gold.

(ii) We have already stated our conclusion that it is desirable to stabilise the rupee at as early a date as practicable at a level which will ensure that it remains a token coin, and will remove the necessity, for further increases in its value to meet further rises in the sterling price of silver. We have also pointed out that such rises might result from further depreciation of sterling. This possibility increases very seriously the difficulty of fixing a sterling value for the rupee which could be maintained with certainty; but if the value of the rupee is fixed in relation to gold and not to sterling, one disturbing cause at least is eliminated, since any rise in the sterling price of silver resulting from further depreciation in sterling would be counter-balanced by a similar automatic rise in the sterling value of the rupee.

(iii) The value which it would be necessary to fix in sterling at the present time, in order that the rupee might have an exchange value exceeding that of its silver content, would be a high one. Under present conditions we do not as we have explained, regard that as a disadvantage. But if at some future time sterling recovers its value and becomes equivalent once more to gold, the sterling value for the rupee imposed by present conditions might be found too high, since that value would have increased in relation to gold, and probably in relation to other commodities, in proportion to the recovery of sterling from its depreciation It may be answered that it

the value is found to be too high, it can be reduced. But any reduction of the value fixed would have to be made by the Legislature or by acts of the Executive, similar in character to those which have enforced successive rises in value, but arbitrary because not dictated by circumstances and therefore specially injurious to commercial confidence. If on the other hand, the value is fixed in relation to gold, it can be fixed with safety at a lower figure ;and although at the present time the corresponding sterling value of the rupee will be no less high than if it had been fixed in sterling, the sterling equivalent will automatically fall in correspondence to any recovery in sterling, and will ultimately coincide with the gold value.

(iv) If the relation of the rupee to sterling is fixed, while sterling varies in relation to gold, it is evident that the relation of the rupee to gold will vary. But if (as we think essential) the rupee and the sovereign are both to remain unlimited legal tender in India, and to be available for circulation, it is necessary that the relation of the rupee to the sovereign should be fixed, since two coins cannot remain in circulation as unlimited legal tender and at the same time stand in a variable relation to one another. The result would be that the relation of the sovereign to gold would vary—in fact, that the sovereign would become a token coin in India, divorced from its bullion value, and rated at a fixed number of rupees. It would follow that the import of sovereigns by the public must be prohibited, that the danger of smuggling and illicit coinage must be incurred, and that gold coin and bullion would not be interchangeable.

(v) In paragraph 65—67 we state our view that it is very desirable to permit the free export and import of gold bullion and coin, and to issue gold coin in India for an equal weight of gold bullion subject only to an appropriate coinage charge. It is clear from what we have said above that these objects can be attained in the near future if the rupee stands in a fixed relation to gold, but not otherwise.

The balance of advantage appears to us for these reasons to be decidedly on the side of fixing the exchange value of the rupee in terms of gold.

Postponement Undesirable.

58. We have now dealt with the various aspects of the question which it was necessary to examine, and we are in a position to formulate our definite recommendations as to the course to be pursued; but before doing so we must give our reasons for not accepting the view, which has been pressed upon us, that no attempt should be made at the present time to fix any definite or final figure for the relation between the rupee and either gold or sterling, but that the policy followed since 1917 should still be pursued. For the development of this view and the explanation of the practical steps which would give effect to it, we must refer to the very able evidence of Sir Lionel Abrahams.

It is true, as we readily admit, that present circumstances are abnormal, and that it is extremely difficult to foresee future developments. This has been demonstrated by the changes in the situation which have taken place since our inquiry began, and this fact was advanced as a reason for recommending that policy should wait upon events, that the exchange value of the rupee should be raised, if a further increase in the price of silver required it, and that it should again be lowered if events proved that the level reached was inconveniently high. But in our terms of reference we are directed to make recommendations with a view "to ensuring a stable gold exchange standard," and we do not think that it would be an adequate discharge of our responsibilities to submit proposals which did not aim at securing stability in the near future, if, as we believe, such a result is attainable. The postponement of a decision which is synonymous with the continuance of the existing uncertainty would be open to serious criticism, and would entail the prolongation of Government control over exchange and over the import of the precious metals into India.

Rate Recommended.

59. We have now arrived at the following conclusion:—

(i) The object should be to restore stability to the rupee, and to re-establish the automatic working of the currency system at as early a date as practicable (para. 36).

(ii) The stable relation to be established should be with gold and not with sterling (para. 57).

(iii) The gold equivalent of the rupee should be sufficiently high to give assurance, so far as is practicable, that the rupee, while retaining its present weight and fineness, will remain a token coin, or in other words, that the bullion value of the silver it contains will not exceed its exchange value (para. 43).

After most careful consideration we are unanimous (with the exception of one of our members, who signs a separate report) in recommending that the stable relation to be established between the rupee and gold should be at the rate of ten rupees to one sovereign, or in other words, at the rate of one rupee to 11.30016 grains of fine gold both for foreign exchange and for internal circulation. While some of our number would have preferred that the rate to be adopted should be nearer to that which has been in force for the last 20 years, we all recognise that no lower rate will attain the objects which we find to be indispensable. Our recommendation accords with the views expressed by the Government of India after they had taken account of the changes in the situation since the preparation of their original proposals. They strongly support the establishment of a fixed relation between the rupee and gold, and the adoption of the rate of ten rupees to one sovereign, and they express the view that this solution "combines a more real stability with maxi-"mum possible assurance of convertibility, "and has, in fact, all the elements of a com-"pletely satisfactory permanent system."

We believe, as we have already stated (para. 43), that strong forces will come into operation to prevent the price of silver rising to a point which will cause the bullion value of the rupee to exceed 2s. (gold). If, however, contrary to our expectation, the price of silver should rise for more than a brief period to such a point, the situation should be met by all other available means rather than by impairing the convertibility of the note issue. In the event of such a rise in the price of silver, the Government might diminish the demands upon them for currency by reducing as far as possible the sale of Council Bills, relying on the free import of gold and silver, which we recommend to provide alternative means of remittance. They would naturally endeavour to meet the demands for metallic currency by the use of gold, and abstain as far as possible from purchasing silver. If, in their judgment, it should be absolutely necessary to purchase silver, they should be prepared to purchase even at a price such that rupees would be coined at a loss.

The principal steps for giving effect to our recommendation are (1) a notification changing the present acquisition rate for imported gold and fixing it at the rate of Rs. 10 to the sovereign, (2) an amendment of the Indian Paper Currency Act and Indian Coinage Act, so as to make the sovereign legal tender for Rs. 10 instead of for Rs. 15, and (3) the withdrawal of the existing undertaking to give Rs. 15 for a sovereign.

In this connection it is necessary to consider whether an opportunity should be given to holders of sovereigns to present them for exchange at the existing rate at the time of the introduction of the new ratio (see para. 69 below).

Other steps necessary as regards.—

(1) sales of Council Drafts and Reverse Councils;

(2) import and export of gold and silver;

(3) coinage;

and also as regards the Paper Currency Reserve and the Gold Standard Reserve, are dealt with in the appropriate paragraphs of this Report.

POSSIBLE OBJECTIONS.

60. Two objections have been raised to the course which we recommend:—

(i) It is suggested that if the sovereign, or the weight of gold in a sovereign is obtainable for Rs. 10 instead of Rs. 15, or even larger number. Indians will regard gold as exceptionally cheap, and will absorb greatly increased quantities. It is possible that the Indian demand may, to some extent, be diverted from silver to gold; but in the present conditions of the supply of the two metals, and the demand for them, we do not regard this necessarily as an evil. At the same time, we emphasise the necessity for using all possible means for encouraging the people of India to employ their savings in more useful and fruitful ways than in the acquisition of precious metal, whether gold or silver.

(ii) It is urged that the existing ratio between gold and silver in India is sanctioned by the law and has been in existence for a considerable period, and that to disturb it will be contrary to sound policy. We only agree in this argument to the extent that the legally established ratio ought not to be modified lightly or on insufficient grounds. The modification is, however, clearly within the competence of the legislature, and if it is necessary in order to remove the grave evils of the present position and to re-establish a sound and automatic currency system, we think it is undoubtedly justified. We believe that it is open to far less objection than any of the other alternative courses that have been suggested.

Drafts and Reverse Councils.

61. We now proceed to consider questions connected with the system of remittance to and from India.

We agree with the Chamberlain Commission in holding that Council Drafts are sold not for the convenience of trade, but to provide the funds needed in London to meet the requirements of the Secretary of State on India's behalf in the widest sense of the term. There is, in our opinion, no obligation to sell drafts to meet all trade demands. If our proposals in paragraph 65 to 67 regarding the free import of gold into India and the maintenance of a gold mint are adopted, the way will be open for the settlement of trade balances by means which are independent of the sale of Council Drafts. India, however, normally enjoys a large favourable balance of trade, and the adjustment of this balance mainly by the import of gold would probably involve the shipment to India of more gold than is actually required for absorption by the public. If, therefore, without inconvenience or with advantage the Secretary of State is in a position to sell drafts in excess of his immediate requirements when a trade demand for them exists, we see no objection to his doing so, provided that due regard is had to the proper location of the reserves, to which we refer later. Such sales would tend to economise the movements of gold, and would provide additional facilities for telegraphic remittance, which is an advantage to trade.

The above observations apply to normal times when the purchase of silver for coinage can be readily effected. So long as the existing difficulties continue it will be advisable to adhere to the system at present in force, according to which the actual amounts of Council Drafts sold weekly are fixed with reference to the Secretary of State's requirements and the capacity of the Government of India to meet them.

MINIMUM RATE.

While sterling continues to be divorced from gold, the fixing of the rupee in terms of gold will involve fluctuations in its sterling equivalent; and the minimum rate for Council Drafts will be fixed from time to time on the basis of the sterling cost of shipping gold to India. When sterling is again equivalent to gold, the minimum rate will remain fixed and the price obtained for Council Drafts will vary between the gold points according to the demand.

REVERSE COUNCILS.

62. The Chamberlain Commission recommended that the Government of India should make a public notification of their intention to sell in India bills on London at a price corresponding to the gold export point, whenever they were asked to do so, to the full extent of their resources. We agree entirely with this recommendation. We are informed that inconvenience has resulted in the past from the necessity of consulting the Secretary of State before offers of reverse remittance were announced, and to ensure public confidence in the system it is desirable that the authorities in India should be in a position to take action without the delay involved by reference to London. We are also informed that facilities for telegraphic remittance, which were first offered in connection with the sales at the outbreak of the war, were greatly appreciated by the commercial community in India. We, therefore, recommend that the Government of India should be authorised to announce, without previous reference to the Secretary of State on each occasion, their readiness to sell weekly a stated amount of Reverse Councils (including telegraphic transfers) during periods of exchange weakness. The rate will, as in the past, be based on the cost of shipping gold from India to the United Kingdom. So long as sterling is divorced from gold, it will not be possible to announce a fixed rate at which sales will uniformally be made, but the Government of India should be prepared to quote the appropriate figure as soon as the demand for remittance from India makes itself apparent. During this period, assuming that our recommendations regarding the exchange value of the rupee are adopted, 10 rupees will purchase the sterling equivalent of one sovereign less a percentage to cover the charges of remittance.

Indian Demand for Precious Metals.

63. We now turn to the policy that should be adopted in regard to the import and export of the precious metals into and from India.

Statistics regarding the imports of gold into India on private account in recent years are shown in paragraph 14. It will be seen that during the five years preceding the war, India's average annual import of gold coin and bullion exceeded £19,000,000.

It has frequently been alleged that an undue proportion of the world's gold supply is absorbed by India. It must be remembered,

however, that the population of India exceeds 315 millions, and that the use of gold (or, alternatively, of silver) plays an important part in social ceremonies sanctioned by religion and tradition. Presents of gold or silver ornaments are obligatory at weddings, and on other ceremonial occasions; and this custom is supported by the practical consideration that a woman, whether Hindu or Moslem, who possesses gold and silver ornaments or coins converted into ornaments, is entitled to hold them as her personal property. It has also always been the habit in India to use the precious metals as a store of value, and to hold savings in this form; nor, until banking and investment facilities have been extended, and the habit of using them has been acquired by the people of India, is it easy to see in what other form savings can be accumulated. We do not, therefore, consider that the quantity of gold taken by India for all purposes in the period before the war was disproportionately large in relation to her economic condition ,and it must be assumed that so long as existing conditions prevail India will continue to require a considerable quantity of gold for the purposes named above.

64. We have previously pointed out that the normal balance of trade makes India a creditor country, and as such she is entitled to require payment for her produce in the form most acceptable to her people. Indeed, India's capacity to draw gold from other countries depends in the last resort on the desire of her customers to secure her produce, and, so long as they continue to take it, India will be in a position to demand gold, in so far as she may prefer payment in this form to the import of commodities or the investment in foreign securities of credits due to her.

We do not wish, however, by these remarks to lend support to any suggestion that the import of precious metals is the most advantageous way by which India can adjust her claims against other countries. The accumulation of stores of gold and silver is an unprofitable method of saving, and it would undoubtedly be to India's own interest, and to the interests of the world at large, for her to employ her wealth in productive directions. We are, therefore, glad to learn that an increasing interest is now being shown by Indians in the promotion of industrial enterprise, and we consider (see para. 73) that facilities for the deposit and investment of savings should be increased in all practicable ways. This may tend ultimately to reduce India's demand for the precious metals.

IMPORT AND EXPORT OF GOLD.

65. Under the Gold Import Act all gold imported into India has to be tendered to Government at a specified rate based on the exchange value of the rupee and the premium on gold. The export of gold is not prohibited, but owing to the fact that gold commands a substantial premium in the Indian bazaar, there is no tendency for it to leave the country under existing conditions. The provisions regarding the import of gold were avowedly enacted under the stress of war and were only intended to be temporary. It is, in our opinion, desirable that the entry of gold into India should be freed from regulation or control by the Government. We accordingly recommend that the Gold Import Act should be repealed as soon as the change in the statutory ratio of the rupee to the sovereign, to which we refer below, has been effected. Movements of gold to and from India would of course continue, as in the past, to be reported for registration and statistical purposes.

GOLD AS CURRENCY.

USE OF GOLD AS CURRENCY.

66. The fixation of the rupee in terms of gold and the disappearance of the internal premium on gold due to the removal of the prohibition on import will again enable gold to circulate as currency. It is, therefore, necessary to consider how far the extended use of gold currency is desirable in India. We agree in principle with the recommendations of the Chamberlain Commission in this connection, but the position has changed in certain respects since the issue of their report, and some modifications in the policy suggested are advisable. We agree with their conclusions that the Government should continue to aim at giving the people the form of currency which they demand, whether rupees, notes, or gold, that the use of the note should be encouraged, that the currency most generally suitable for the internal needs of India consists of rupees and notes, and that it would not be to India's advantage actively to encourage the increased use of gold in the internal circulation. We also share the view that gold can be more advantageously employed in the Government reserves, where it is available for meeting demands for foreign remittance, than in the hands of the people in the form of currency. For some time, however, it may be difficult to meet all demands for metallic currency in rupees, and a more extensive use of gold may be necessary to ensure confidence in the note issue. We understand that on recent occasions the issue of gold coin by the Government has been

looked upon in certain parts of India as an indication that the Government were in difficulties regarding the provision of metallic currency. In order to avoid creating this impression by exceptional issues, we think that so long as the purchase of adequate supplies of silver continues to be difficult it would be advisable for the Government, as one of the normal methods for meeting demands for currency, to issue gold coin in moderate quantities. When the supply of silver has ceased to be difficult, the necessity for the issue of gold coin will diminish, but it is probable that there will always be a demand for gold in certain parts of India. We consider, therefore, that the Government of India should maintain their pre-war practice of making gold coin available when it is demanded by the public.

FACILITIES FOR MINTING.

67. In order that gold currency may be available when required it is important to provide facilities in India for the conversion of gold bullion into legal tender coin. These facilities might be given by the establishment of an Indian gold mint, which would mint Indian gold coins such as the gold mohur, or by the re-opening of the branch of the Royal Mint in Bombay. After careful consideration we have come to the conclusion that it will be more advantageous to India to continue to use the form of gold currency to which she has become accustomed and which, on account of its wide circulation, is a universally recognised medium for the settlement of external obligations. We therefore recommend that the branch of the Royal Mint which was opened in Bombay during the war for the coinage of sovereigns and half-sovereigns and has since been temporarily closed, should be re-opened, and that arrangements similar to those in force in the United Kingdom should be made for the receipt of gold bullion from the public for coinage. The Government of India should announce its readiness to receive gold bullion from the public, whether refined or not, and to issue gold coin in exchange at the rate of one sovereign for 113.0016 grains of fine gold, subject to a small coinage charge. This undertaking would not of course require the constant operation of the gold mint, if the demand for the coinage of gold did not justify it. The issue of gold coin in exchange for unrefined gold makes a gold refinery necessary. If the need is not met by private enterprise, we recommend that facilities should be given to the public by which they may be able to have gold refined at the Government refinery on payment of charges sufficient to cover the cost of the operation.

68. Sovereigns and half-sovereigns have been for many years legal tender in India, and, as we have stated in paragraph 6, the Government of India have undertaken by notification to issue rupees in exchange for sovereigns presented to them. In normal times, and whenever the supplies of silver permit, the Government of India will doubtless offer all facilities for the conversion of legal tender gold into legal tender silver coin and *vice versa*; but, in view of the present shortage of silver, we consider that the obligation to give rupees for sovereigns should be withdrawn.

EXISTING HOLDERS.

69. Under the scheme we have advocated the gold content of the sovereign will be exchangeable in India for Rs. 10, and in order to put this rate in force it will be necessary to amend the status under which the sovereign is rated at Rs. 15, and to reduce the rate to Rs. 10. It will also be necessary to cancel the notification under which the Government have undertaken to give Rs. 15 for all sovereigns tendered at the Reserve Treasuries. The question thus arises as to the treatment that should be accorded to the present holders of sovereigns in India. It is undoubtedly open to the Government to enact through the competent legislature that the rate at which the sovereign is legal tender should be reduced from Rs. 15 to Rs. 10 and to cancel the notification to which we have referred. We do not recognise any legal obligation on the part of the Government to indemnify holders of sovereigns from loss through change of rate, but we think that reasonable opportunities should be given to the public to exchange sovereigns in their possession at the rate of Rs. 15 at the time of the introduction of the new ratio. In order to reduce the period of transition, which must necessarily be attended by obvious risks and inconveniences, the offer should run for a short period only, and if the impending change is widely notified and opportunities for the tender of sovereigns are made available at a large number of places (which would include all Treasuries and possibly all Sub-Treasuries), we hope that it may be found practicable to limit the period to a calendar month. The period suggested is short, and its precise duration should be determined on the discretion of the Government of India; but we feel strongly that action, when taken, should be prompt. In order to prevent an excessive call upon their resources of silver, the Government should reserve to themselves the option of redeeming sovereigns in gold coin at the rate corresponding to the new ratio (viz., 1⅓ sovereigns for

each sovereign), to be payable after the termination of the period of redemption, and to be represented in the meantime by certificates or other suitable instruments created for the purpose.

There would be advantages in carrying out this operation at an early date so that the imports of gold coin and bullion into India may be free from control, and that the sovereign may be put into circulation as the equivalent of Rs. 10. But it must be for the Government to determine the detailed steps by which effect should be given to our suggestions.

The gold mohurs which were coined and issued during the war as the equivalent of 15 rupees should also be redeemed at that rate either now or at some later period as may be convenient. After a reasonable opportunity for redemption has been given, any remaining unredeemed should be demonetised."

Import and Export of Silver.

70. We have already indicated that we are in favour of the removal of Government intervention in the free flow of the precious metals to and from India as soon as practicable. The import of silver was prohibited at a time of abnormal demand for currency and limitation of supply with the object of preventing private buyers in India from competing in the silver market with the Secretary of State. It is difficult to estimate how far the removal of their competition has facilitated the silver purchases of the Secretary of State during the last two years. The evidence we have taken suggests that, in spite of the prohibition of the melting of silver coin, the melting of rupees has taken place on a large scale. When the bullion value of the rupee approximates closely to its exchange value the most economical method of obtaining silver in India is by melting coin. In so far as the demand for silver for social and industrial purposes, enhanced by the scarcity of gold, has been met in this way, the effect of the prohibition of private imports was to increase the amount of silver which the Secretary of State had to purchase. If the restrictions on gold are removed the demand for silver may be expected to decrease, but a considerable quantity will always be required for social and industrial purposes. We consider that the disadvantages of meeting the public demand through Government agency by the indirect and expensive method of issuing additional currency, outweighs any advantage which may be gained in respect of the Secretary of State's purchases. We therefore recommend the removal of the prohibition on the import of silver as soon as is convenient.

IMPORT DUTY ON SILVER.

71. Prior to the year 1910 silver bullion and coin other than current coin of the Government of India were included in the general tariff schedule of articles liable to an import duty of 5 per cent. *ad valorem*. In that year it was necessary to raise additional taxation, and it was decided that silver was a luxury article on which an additional import duty might suitably be imposed. The rate was accordingly raised to four annas per ounce. At that time the price of silver was such that the additional duty on silver could have no influence on the currency system, but the rise in the price of silver to a height at which the bullion value of the rupee approximates to its exchange value introduces fresh considerations; for whenever the exchange value of the rupee does not exceed the bullion value by the amount of the duty, it is cheaper to obtain silver for the arts in India by melting the currency than by importing silver bullion. So long, therefore, as the divergence between the bullion value and the exchange value of the rupee is not large, the retention of the import duty may throw upon the Government of India the burden of providing rupees in excess of the needs for currency purposes. The removal of the duty has also been advocated on the ground that it imposes an unfair burden on the poorer classes, to whom a certain quantity of ornaments is a social necessity rather than a luxury. We do not attach weight to this argument, but we believe that there is a strong feeling in India against the retention of the duty in that it is an obstacle to the establishment of a world market for silver in Bombay, and places the Indian consumer of silver at a disadvantage in comparison with that of the population of other countries. The Government of India would prefer to defer consideration of the removal of the duty until the results of the relaxation of the control over the movement of the precious metals have been observed, but we see no reason for the postponement of the decision on the point of principle involved. Since the prohibition of the import of silver, the revenues of the Government of India have been deprived of the yield from the silver duty, which was about one crore annually before the war, and the gap has been filled from other sources. The abolition of the duty at the present time would therefore involve no readjustment of the burden of

taxation. For these reasons we recommend that when the prohibition of import of silver is removed, the duty should also be removed, unless in the opinion of the Government of India the fiscal position demands its retention.

RETENTION OF CONTROL.

72. As regards the export of silver, we are unable to recommend the removal of the prohibition at present, although we think that the removal of all restrictions is an ideal to be attained as soon as circumstances permit. As long as the bullion value of the rupee is near its exchange value, it is possible that the export of silver rupees or silver obtained by melting rupees will be a profitable transaction, and it is necessary that Government should be in a position to protect the currency from depletion by export. We recommend, therefore, that the export of silver, except under licence, should be prohibited, until changed conditions again definitely establish the rupee as an over-valued token coin. Meanwhile it is important that the production of silver in India should not be discouraged by a measure which is intended only to protect the currency. We understand that silver mined in India is now purchased by the Government of India at rates fixed by contract with the producers. We hope that so long as the Government of India require silver this arrangement will be continued on suitable terms; but if at any time before the removal of the export prohibition the continuance of the purchase by Government of silver mined in India should be unnecessary or impracticable, we consider that the producers should be permitted to export freely under licence the silver produced from their mines.

FACILITIES FOR SAVING AND INVESTMENT.

73. We have already referred to the extensive use in India of the precious metals, mainly in the form of currency, as a store of value. It has been urged that this practice is largely due to the inadequacy of the disposal of savings in a manner which will enable them to be used productively. We, therefore, welcome the recent announcement of the Government of India that a feature of the scheme for the amalgamation of the Presidency Banks is the opening of at least 100 new branches within the next five years. We recommend that this policy should be actively pursued. By the extension of the activities of the amalgamated Presidency Banks and other sound banking institutions in India, we hope that facilities for the deposit of savings will gradually be made available in all headquarters of administrative districts and other towns where no banks have yet been established. We suggest also that the Government of India should consider whether it is practicable to abolish the existing stamp duty on cheques.

An extension of banking facilities, however, on such a scale as would attract deposits from the remoter areas is unlikely in the near future, and we think, therefore, that the rural population should be encouraged to take fuller advantage of the opportunities for making interest-bearing deposits in Co-operative Credit Societies and the Post Office Savings Banks. We are impressed by the comparatively insignificant figure of the total deposits in the Post Office Savings Banks, amounting to only Rs. 24½ crores on 31st July, 1914, before the condition that ensued on the outbreak of war led to the heavy withdrawals referred to in paragraph 9. We understand that the substantial increase in deposits in the years 1912-13 and 1913-14, amounting to over four crores, was due mainly to the grant of additional facilities, and we recommend that the Government of India should examine how far, notwithstanding the admitted administrative difficulties, it may be possible to improve the present procedure for the deposit and withdrawal of money, and to increase the number of post offices conducting savings bank business.

In addition, we advise that all possible facilities should be made available for the investment of savings in Government Loans. In particular, in view of the success which has attended the Government of India's war borrowings through the Post Office, notably in the form of cash certificates, we suggest that a Postal Section should be retained as part of the normal borrowing system of India.

It has been suggested to us that Indian investors would be prepared to purchase sterling securities of the Indian Government if facilities were given for the purpose. We are not in a position to judge how far this proposal is practicable or expedient, but we desire to bring it to the notice of the Secretary of State and the Government of India.

SILVER PURCHASES.

74. Before leaving the subject of the precious metals, it will be convenient to deal with the criticisms of certain witnesses regarding the conditions under which purchases of silver for coinage have been made. The allegations of the critics are to the effect that the method of purchase through a broker, mainly in the London market, is unsatisfactory, and has resulted in pur-

chases being made at an unnecessarily high price; and that purchases by open tender in India would give better results. We have considered the subject carefully, and without entering into unnecessary details, we are satisfied that the purchases of the Secretary of State, which are made in the same manner as the purchases of His Majesty's Mint, many foreign Governments, and the banks concerned in the supply of silver to the Far East, are suitably conducted. We do not, therefore, make any recommendation for modifying the present practice, though we have no wish to suggest any limitation of the freedom which the Secretary of State now enjoys of making purchases in India or elsewhere than in the United Kingdom should he think it advantageous to do so.

PAPER CURRENCY RESERVE.

75. In paragraph 28 we have referred to the large expansion of the note-issue during the war. This expansion has been in great part due to special causes arising from the war; but we believe that it has been beneficial to India, and we should welcome any further action that might tend to foster the note-using habit, especially under present conditions when the purchase of silver for coinage is attended with serious difficulty. But the continued popularity of the note can only be assured if its convertibility is guaranteed beyond all possible doubt. Our recommendations regarding the note issue have accordingly been framed with the express purpose of justifying the confidence of the Indian public in the note by the provision of an adequate metallic reserve and the grant of ample facilities for converting the note into coin. We also take into account the necessity of avoiding on the one hand the inconveniences attending an inelastic currency, and on the other the risks of inflation arising from a currency which can be expanded with undue ease.

76. At the outbreak of war the limit to the invested portion of the Paper Currency Reserve was 14 crores, of which 4 crores might be held in sterling securities, defined as "Securities of the United Kingdom of Great "Britain and Ireland or securities issued by "the Secretary of State for India in Council "under the authority of Act of Parliament, "and charged on the revenues of India." The great expansion of the note issue during the war, coupled with the difficulty of obtaining gold or silver, made it necessary to enlarge these limits. The limits of investment were modified by no less than nine Acts and Ordinances, and the statutory maximum is now 120 crores, of which 20 crores may be held in securities of the Government of India. The increased powers of investment taken since the outbreak of the war are temporary and will, unless re-enacted, lapse six months after the official date for the termination of the war.

77. The Chamberlain Commission commented in paragraphs 103 to 105 of their Report on the inelasticity of the Indian paper currency system. The maximum limit for the invested portion of the reserve is fixed by Statute, and when that limit is reached any further increase in the note-issue requires the deposit of an exactly equal amount of gold or silver in the reserve. Special application to the legislature is necessary when an increase in the circulation renders it expedient to increase the amount of the invested reserve. It may be added that legislation would equally be required if a decrease in the circulation made it desirable to reduce the limit of investment. We recognise the special need for caution in dealing with the note-issue in such a country as India, where a large part of the population is illiterate and the extended use of paper currency is a habit of very recent growth, but we think it essential to introduce some elasticity into the system, and at the same time to obviate the necessity for constant fresh applications to the legislature as the circulation grows. Both these objects can be attained, if instead of laying down that the invested portion of the reserve must not exceed a fixed maximum, the legislature prescribes that it shall not exceed a maximum percentage of the total issue; or, alternatively, that the metallic portion shall not fall below a minimum percentage of the total issue. In recommending that this method should be adopted we find ourselves in accord in principle with the views of the Chamberlain Commission, and also with those expressed in the memorandum annexed to the statement submitted on behalf of the Government of India.

RESERVE TO BE 40 PER CENT.

78. The Chamberlain Commission recommended that the fiduciary portion of the Paper Currency Reserve, which at the time of their Report stood at 14 crores, should be increased at once to 20 crores and should thereafter be fixed at a maximum of the amount of notes held by Government in the Reserve Treasuries, plus one-third of the net circulation. The large increase in the note circulation that has taken place during the course of the war and subsequently has modified the position as it existed when the Commission reported. Under their recommendation it would be necessary that on the present basis of circulation the metallic re-

serve should amount to 119 crores of rupees, as compared with 80 crores so held at the present time. We do not consider that so large a reserve is required for ensuring the convertibility of the note issue, especially when it is remembered that in the case of any drain arising from demands for foreign remittance the Gold Standard Reserve is also available. We recommend that the statutory minimum for the metallic portion of the reserve should be 40 per cent. of the gross circulation.

It would, of course, be desirable to maintain in the metallic reserve a substantial margin above the statutory minimum, especially at the beginning of the busy season, which always brings a demand for issues of coin.

It might appear that our recommendation is less cautious than that put forward by Mr. Howard, who proposes for the metallic reserve a minimum proportion of 50 per cent. But he applies the percentage not to the circulation of the moment, but to the average of the gross circulation on the closing days of the three preceding financial years. In times when the circulation is growing rapidly the figure so ascertained is greatly reduced. At the present time, for instance, Mr. Howard's proposal would fix the minimum metallic reserve at 56½ crores, while our recommendation would make it nearly 72 crores.

79. As regards the composition of the fiduciary portion of the reserve, we recommend that the amount to be held in securities issued by the Government of India should be limited to 20 crores, the figure at present permissible under the temporary legislation now in force, and that the balance should be held in securities of other Governments comprised within the British Empire. Of the amount so held not more than 10 crores should be invested in securities with more than one year's maturity, and any securities so held should be redeemable at a fixed date. The balance of the invested portion of the reserve over and above the 30 crores already provided for should be held in short-date securities with not more than one year's maturity, issued by Governments within the British Empire other than the Government of India. The operation of our recommendations may be illustrated by the following figures exhibiting the composition of the reserve as it stood on 30th November 1919, as it would stand if the invested portion stood at the maximum permitted under the existing law and consequently if the metallic reserve was at the minimum permissible, and as it would stand if the metallic reserve did not exceed the minimum permitted under our recommendations:—

—	Gross Note Circulation.	Composition of Reserve (Lakhs of Rupees).				Percentage of Total Metallic Reserve to Gross Note Circulation.
		Silver	Gold	Securities Indian.	Securities British	
Actual figures for 30th November 1919	179,67	47.44	32,70	17,03	82,50	44·6
Figures showing maximum fiduciary issue under present law	179.67	59,67		20,00	100,00	33·2
Figures showing maximum fiduciary issue under proposals in report	179,67	71,87		20,00	87,80	40

These are our proposals regarding the permanent constitution of the Paper Currency Reserve, but we recognise that it may not be possible to maintain continuously such a large proportion of the reserve in metal in the immediate future. We accordingly recommend that, when permanent legislation is introduced in replacement of the present temporary provisions, authority for retaining for a limited period the existing permissive maximum of 120 crores for the fiduciary issue should be sought.

The change in the gold equivalent of the rupee will involve a revaluation of the sterling investments and gold now held in the reserve. We recommend that the sterling investments should be valued at the rate of 10 rupees to the £, no account being taken for this purpose of the temporary depreciation of sterling in terms of gold. The revaluation of the sterling investments and gold at 2s. to the rupee will lead to a deficiency at once, but we are of opinion that any savings or profits arising from the rise in the equivalent of the rupee from 1s. 4d. to 2s. gold, such as the saving in the remittances made to meet the direct Home expenditure of the Government of India, will supply a suitable means for discharging this liability in a limited number of years.

SEASONAL DEMAND.

80. While our recommendations introduce a measure of elasticity into the Indian note issue, we think it desirable to provide for a further limited power of expansion with a special view to meeting the seasonal demand for additional currency which is normal in India. The proposals formulated by Mr. Howard contemplate that the note-issue should be based in part upon commercial bills of exchange. We have given careful consideration to this plan, with special reference to its application on the largest scale

as the basis of the Federal Reserve Note system in the United States of America; and we recommend that it should be tried experimentally in India on a small scale, as the basis for the special power of expansion which we find to be advisable. The requirements of the case would, we think, be met by authorising in the first instance the issue of notes up to 5 crores on the security of commercial bills of exchange in addition to the normal issue. The issue would take the form of loans to the Presidency Banks on the collateral security of bills endorsed by the Presidency Banks and having a maturity not exceeding 90 days. The interest charged to the banks for such advances should be not less than 8 per cent. per annum. The advances should be outside any loans made from Government Treasury balances. The bills tendered as collateral should be bona fide commercial bills against goods under export, not only because such bills would lead to the automatic retirement of the emergency note issue on their maturity, but also because such bills are more commercial transaction than internal bills easily identifiable as representing a definite commercial transaction than internal bills which may be created for purposes of finance or against goods held for speculative transactions. If the difficulty of connecting internal bills with definite transactions in commodities can be overcome, we should see no objection hereafter to authorising the tender of such bills as collatoral in addition to export bills, but we think that at the inception of a scheme which is admittedly experimental it would be wiser to authorise the tender of export bills only.

LOCATION OF RESERVE.

81. The location of the Paper Currency Reserve has given rise to considerable discussion in the past. The main facts of the position may be stated as follows: The reserve exists primarily for the redemption of notes, and the proper place for holding the greater part of the reserve must therefore be in India where the notes may have to be met. The silver reserves should, therefore, as in the past, be normally held in India, but silver under purchase or in the course of shipment should be treated as part of the reserve pending its arrival in India.

The gold also in the Paper Currency Reserve should normally be held in India; but some Paper Currency Gold may at times be held in London, either because it has been purchased there and is awaiting shipment, or because it is held in anticipation of its use in payment for purchases of silver.

Of the securities held in the Paper Currency Reserve, the Government of India's securities would naturally be held in India, while the remainder would be held in the United Kingdom where they would be redeemable or realisable in event of need.

ENCASHMENT.

82. As soon as circumstances permit, free facilities for the encashment of notes should be given, and the restrictions imposed during the course of the war should be withdrawn. We do not suggest that the legal obligation of Government to encash notes should be extended beyond the Currency Offices, but we are satisfied that the additional facilities provided by the Government have tended to encourage confidence in the note issue, and we would, therefore, welcome their restoration, although we recognise that this may not be practicable at the moment. The obligation of the Government to redeem its notes should be to redeem them in full legal tender coin. It is not necessary that the public should have the option of demanding gold or silver when they present notes. The choice of the metal should be, as it is now, at the option of the Government, who would, no doubt, in normal conditions endeavour to make payment in whatever form of currency is preferred by the tenderer of the note.

Gold Standard Reserve

83. The Chamberlain Commission held that no limit could be fixed at the time when they reported to the amount up to which the Gold Standard Reserve should be accumulated, and that the profits on the coinage of rupees should continue to be credited exclusively to the reserve. During the war the circumstances have been abnormal, and we consider that it will be advisable to await the return of normal conditions before fixing any maximum figure for the reserve. In reaching this conclusion we are also influenced by the proposal we have made in regard to the new ratio for the rupee. So long as prices throughout the world remain at or about the present level, we believe that India will maintain a prosperous export trade, and that the present strength of the Gold Standard Reserve, assisted by the other resources of the rupee at the point we suggest. But if there were a sudden fall in world prices it is possible, as we have pointed out in paragraph 51, that the normal current of Indian trade might be affected for a period, and that a heavier call might be made on the resources for supporting exchange than has occurred in the past. We hold, therefore, that when profits again accrue on the coinage of rupees they should be credited in their entirety to the reserve.

COMPOSITION OF RESERVE.

84. The recommendation of the Chamberlain Commission that the silver branch of the Gold Standard Reserve, which in June 1914 amounted to 6 crores of rupees, should be abolished, has already been carried out.

At present the reserve is held almost entirely in securities, and on the 30th November, 1919, was constituted as follows, the figure given representing in each case the face value of the security:—

	£
British Treasury Bills, maturing between December, 1919, and March, 1920	8,219,000
Exchequer Bonds, redeemable between February, 1920, and October, 1921	16,199,300
National War Bonds, redeemable 1st October, 1922	7,500,000
Five per cent War Loan 1929-47	3,762,181
Local Loans, 3 per cent. Stock	200,000
Irish Land Stock, 2½ per cent.	438,720
Transvaal Government 3 per cent. Guaranteed Stock, 1923-53	1,092,223
	37,411,224
Cash	27,093
Total	37,438,317

The Chamberlain Commission were of opinion that a considerable portion of the reserve should be held in gold, and suggested that the total gold holding should be raised as opportunity offered to £15,000,000 and that the authorities should thereafter aim at keeping one-half of the total reserve in actual gold. We agree in principle that the reserve should contain a considerable proportion of gold, but we do not anticipate that under the changed conditions a large gold holding will be attainable for some years, and we feel that in the present state of the note issue such gold as the Government of India can obtain should be added to the Paper Currency Reserve rather than to the Gold Standard Reserve. At the present moment, therefore, the most satisfactory course lies in keeping the reserve as liquid as possible by an ample holding of securities with early dates of maturity. This condition is secured under the present scheme of investment. From the statement given above it will be seen that, with the exception of about £5,500,000, the securities in the reserve are redeemable by October, 1922, at the latest. We are of opinion that the amount of securities with a maturity exceeding three years should not be increased, and that the authorities should aim at holding all the invested portion of the reserve in securities issued by Governments within the British Empire (other than the Government of India), and having a fixed date of maturity of not more than 12 months.

LOCATION OF RESERVE.

85. The object for which the Gold Standard Reserve exists is to afford protection against a fall in exchange by meeting demands for sterling remittance to London; and it is evident that its resources will be most readily available for this purpose if they are held in London. This consideration has governed the location of the fund hitherto, and was considered by the Chamberlain Commission to be decisive.

There is, however, a strong sentiment in India in favour of the location of the whole, or at any rate a large part, of the reserve in India. In currency matters the possession of public confidence is an asset of great value, and we therefore think it advisable to comply with the Indian demand, so far as this can be done without detracting from the utility of the fund for the purposes for which it exists. Gold in India can be made available for the purpose of foreign remittance, either by export or by transfer to the Paper Currency Reserve in India against a corresponding release of Paper Currency assets in the United Kingdom or, in circumstances of urgency, by arranging to earmark it for the Bank of England. We consider, therefore, that a portion of the gold in the Gold Standard Reserve should be held in India; but the gold so held should not exceed one-half of the total and steps should be taken to ensure that it is not made available to the public except for the purpose of export.

The sterling investments of the Gold Standard Reserve (including cash on deposit) should, as in the past, continue to be held in London.

86. Our colleague, Mr. Dalal, submits a separate report. While we regret that he does not share our conclusions, we wish to record our appreciation of the assistance which we have derived from his knowledge and experience.

Summary of Conclusions.

87. We now proceed to summarise the main conclusions at which we have arrived.

(i) It is desirable to restore stability to the rupee and to re-establish the automatic working of the Indian currency system. (Para. 36.)

(ii) The reduction of the fineness or weight of the rupee (para. 38), the issue of 2- or 3-rupee coins of lower proportional silver content than the present rupee (para. 39), or the issue of a nickel rupee (para. 40), are expedients that cannot be recommended.

If the legal tender limit of one rupee for the 8-anna nickel coin should prove an obstacle to its free circulation the question of raising the limit to Rs. 5 or Rs. 10 should be considered. (Para. 40.)

(iii) The maintenance of the convertibility of the note issue is essential, and proposals that do not adequately protect the Indian paper currency from the risk of becoming inconvertible cannot be entertained. (Para. 41.)

(iv) The rise in exchange, in so far as it has checked and mitigated the rise in Indian prices, has been to the advantage of the country as a whole, and it is desirable to secure the continuance of this benefit. (Para. 50.)

(v) Indian trade is not likely to suffer any permanent injury from the fixing of exchange at a high level.

If, contrary to expectation, a great and rapid fall in world prices were to take place, and if the costs of production in India fail to adjust themselves with equal rapidity to the lower level of prices, then it might be necessary to consider the problem afresh. (Para. 51.)

(vi) The development of Indian industry would not be seriously hampered by a high rate of exchange. (Para. 52).

(vii) The gain to India of a high rate of exchange for meeting the Home charges is an incidental advantage that must be taken into consideration. (Para. 53.)

(viii) To postpone fixing a stable rate of exchange would be open to serious criticism and entail prolongation of Government control. (Para. 58).

(ix) The balance of advantage is decidedly on the side of fixing the exchange value of the rupee in terms of gold rather than in terms of sterling. (Para. 56-7.)

(x) The stable relation to be established between the rupee and gold should be at the rate of Rs. 10 to one sovereign, or, in other words, at the rate of one rupee for 11.30016 grains of fine gold, both for foreign exchange and for internal circulation. (Para. 59.)

(xi) If silver rises for more than a brief period above the parity of 2s. (gold), the situation should be met by all other available means rather than by impairing the convertibility of the note issue. Such measures might be (a) reduction of sale of Council bills; (b) abstention from purchase of silver; (c) use of gold to meet demands for metallic currency. If it should be absolutely necessary to purchase silver, the Government should be prepared to purchase even at a price such that rupees would be coined at a loss. (Para. 59.)

(xii) Council Drafts are primarily sold not for the convenience of trade but to provide for the Home charges in the widest sense of the term. There is no obligation to sell drafts to meet all trade demands; but, if without inconvenience or with advantage the Secretary of State is in a position to sell drafts in excess of his immediate needs, when a trade demand for them exists, there is no objection to his doing so, subject to due regard being paid to the principles governing the location of the reserves.

Council Drafts should be sold as now by open tender at competitive rates, a minimum rate being fixed from time to time on the basis of the sterling cost of shipping gold to India. At present this rate will vary; but when sterling is again equivalent to gold, it will remain uniform. (Para. 61.)

(xiii) The Government of India should be authorised to announce, without previous reference to the Secretary of State on each occasion, their readiness to sell weekly a stated amount of Reverse Councils (including telegraphic transfers) during periods of exchange weakness at a price based on the cost of shipping gold from India to the United Kingdom. (Para. 62.)

(xiv) The quantity of gold taken by India for all purposes in the period before the war was not disproportionately large having regard to her social customs and economic position; but more productive methods for employing wealth should be encouraged. (Para. 63-4.)

(xv) The import and export of gold to and from India should be free from Government control. (Para. 65.)

(xvi) The Government should continue to aim at giving the people the form of currency

which they demand, whether rupees, notes, or gold; but gold can be employed to the best advantage in the Government reserves where it is available for meeting the demand for foreign remittance.

It would not be to India's advantage actively to encourage the increased use of gold in the internal circulation, but it may for some time be difficult to meet all demands for metallic currency in rupees, and a more extensive use of gold may be necessary. In order that confidence may not be disturbed by exceptional issues, the issue of gold coin in moderate quantities should be one of the normal methods of meeting demands for currency. (Para. 66.)

(xvii) The Bombay branch of the Royal Mint should be re-opened for the coinage of sovereigns and half sovereigns and facilities should be afforded to the public for the coinage of gold bullion and for the refining of gold. (Para. 67.)

(xviii) The obligation of the Government to give rupees for sovereigns should be withdrawn. (Para. 68.)

(xix) Opportunities should be afforded to the public to exchange sovereigns in their possession at the rate of 15 rupees per sovereign at the time of the introduction of the new ratio. Similar opportunities should be given to holders of the gold mohur which should eventually be demobilised. (Para. 69.)

(xx) The prohibition on the import of silver should be removed as soon as is convenient. (Para. 70.)

(xxi) When the prohibition on the import of silver is removed, the import duty should also be removed, unless the fiscal position demands its retention. (Para. 71.)

(xxii) The prohibition on the export of silver should be retained for the present with a view to the protection of the silver currency from depletion by export.

If the silver mined in India should cease to be purchased by the Government, its export should be permitted under licence. (Para. 72.)

(xxiii) Improved banking facilities and increased opportunities for the investment of savings should be afforded. (Para. 73.)

(xxiv) No recommendations is made for modifying the present practice regulating the purchase of silver for coinage. (Para. 74.)

(xxv) The statutory minimum for the metallic portion of the Paper Currency Reserve should be 40 per cent. of the gross circulation.

As regards the fiduciary portion of the reserve, the holding of securities issued by the Government of India should be limited to 20 crores. The balance should be held in securities of other Governments comprised within the British Empire, and of the amount so held not more than 10 crores should have more than one year's maturity, and all should be redeemable at a fixed date. The balance of the invested portion above these 30 crores should be held in short-dated securities, with not more than one year's maturity, issued by Governments within the British Empire.

The existing permissive maximum of 120 crores should be retained for a limited period.

The sterling investments and gold in the Paper Currency Reserve should be revalued at 2s. to the rupee. The depreciation which will result from this revaluation, cannot be made good at once, but any savings resulting from the rise in exchange will afford a suitable means of discharging this liability in a limited number of years. (Paras. 78, 79.)

(xxvi) With a view to meeting the seasonal demand for additional currency, provision should be made for the issue of notes up to five crores over and above the normal fiduciary issue as loans to the Presidency Banks on the security of export bills of exchange. (Para. 80.)

(xxvii) The silver and gold in the Paper Currency Reserve should be held in India except for transitory purposes. (Para. 81.)

(xxviii) As soon as circumstances permit, free facilities for the encashment of notes should be given, and the restrictions imposed during the war should be withdrawn. The Government should have the option of redeeming its notes in full legal tender gold or silver coin. (Para. 82.)

(xxix) No limit can yet be fixed to the amount up to which the Gold Standard Reserve should be accumulated and when profits again accrue on the coinage or rupees they should be credited in their entirety to the reserve. (Para. 83.)

(xxx) Under present conditions Government should hold such gold as they obtain in the Paper Currency Reserve rather than in the Gold Standard Reserve. The Gold Standard Reserve should when practicable contain a considerable proportion of gold; but the most satisfactory course at present lies in keeping the reserve as liquid as possible by the holding of securities with early dates of maturity.

The amount of securities in the reserve with a maturity exceeding three years should not be increased, and the aim should be to hold all the invested portion of the reserve in securities issued by Governments within the British Empire (other than the Government of India) and having a fixed

date of maturity of not more than 12 months. (Para. 84.)

(xxxi) A portion of the gold in the Gold Standard Reserve, not exceeding one half, should be held in India; the sterling investments should continue to be held in London. (Para. 85.)

88. We desire to place on record our high appreciation of the services rendered by Mr. C. H. Kisch, C.B., and Mr. H. Denning, I.C.S., as Secretaries to the Committee. They have discharged the duties entrusted to them with unfailing promptness and courtesy, and their valuable assistance has greatly facilitated our enquiry.

(Signed.) H. BABINGTON SMITH,
CHALMERS.
MARSHALL REID.
J. B. BRUNYATE.
F. C. GOODENOUGH.
C. S. ADDIS.
C. T. NEEDHAM.
M. M. S. GUBBAY.
W. B. HUNTER.
T. W. McMORRAN.

C. H. Kisch,
H. Denning,
Secretaries.

Dated, 22nd day of December, 1919.

MINORITY REPORT.

Recommendations.

Mr. Dadabhai Merwanji Dalal writes a Minority Report in which he says:—

1. I regret that the divergence of opinion between my colleagues on the Committee and myself on vital currency principles is so great as to render it impossible for me to concur with the views of the majority.

2. The tragedy of the great war in its world-wide effects has dealt very unequally with different countries. To India as a whole it brought a period of great economic prosperity, because India was able to supply produce and material which were urgently required in connection with the prosecution of the war, besides taking a full active part in the conflict. Notwithstanding this prosperity, which might have been expected to increase her financial strength, India has been called upon to face a veritable revolution in her currency arrangements which must cause widespread and lasting hardship amongst the masses of the people of India.

3. This revolution has been brought about by the executive action of the authorities by means of raising the sterling rate of exchange. The only occasion on which this Committee were consulted regarding the changes made was when the rate was altered from 2s. to 2s. 2d. Against this alteration I felt it to be my duty to protest.

4. The rate of exchange was raised by stages from the normal rate of 1s. 4d. to 2s. 4d., and the reason assigned was that, owing to the rise in the price of silver, the bullion value of the rupee was above the rate fixed from time to time in relation to sterling. But that reason cannot be held to be the sole reason, since even if the price of silver should fall, the intention is to maintain the rate of exchange at a much higher level than 1s. 4d.

5. I cannot acquiesce in the great change in the money arrangements of India which must accompany this alteration in the rate of exchange. The legally established money standard is the sovereign, with rupees definitely related thereto at the rate of 15 to 1. That standard ratio has been broken by the raising of the rate of exchange, and I hold that it is vitally important that that ratio should be maintained.

6. In my opinion the reason given for raising the rate of exchange is altogether inadequate. The rise in the price of silver could have been prevented by removing the embargo on exports of silver from India after the war had ended, and it was after the war that the greater part of the rise in exchange was brought into force. India could easily have spared silver for export; such exports would have been profitable to her, and they would have prevented the great rise in the price of silver upon which so much has been made to depend through the raising of the rate of exchange. It was chiefly because the export of silver from India was prohibited, and because India was made a potential buyer instead of a seller, that the silver markets were inflamed and the price was raised.

7. Even if silver exports from India were not considered desirable there was still no occasion for raising the rate of exchange after the war because of the rise in the price of silver. It would only have been necessary to stop the sale of rupee bills by Government in excess of their own Treasury requirements and leave the balance of trade to be adjusted by other means than silver.

THE PAPER CURRENCY.

8. There was one important obstacle to the removal of the embargo on silver exports. The paper currency had been heavily

watered by the issue of notes not backed by coin but by British Treasury bills held in London. As a war measure and a temporary expedient to meet the difficulties of the time this might have been excused. After the war, however, this temporary expedient had the effect of blocking the removal of the embargo on silver exports by providing the only strong reason for retaining it, namely, the protection of the paper currency coin reserves against withdrawals of silver for export. This temporary expedient, therefore, turned to the permanent disadvantage of India when it provided a reason for retaining the embargo. But the necessity for protecting in this way the paper currency coin reserves was due to the very artificial conditions created by the extensive watering of the note issue, and consequently the need for the embargo was artificial.

9. As long as a world-wide embargo on gold exports existed a rise to some extent in the rate of exchange could not, perhaps, be temporarily avoided; but when the United States became a free market for gold on the 9th June, 1919, and the gold production of South Africa became available to the highest bidders in London from the 18th July, 1919, the need for further raising the exchange rate from 1s. 8d. by four stages to 2s. 4d. was absolutely uncalled for.

10. These new currency arrangements must, if continued, have disastrous consequences to India and to the people of India. They must seriously disturb the relations existing between creditor and debtor. They will cause dislocation and a set-back to several Indian industries and vast continuous losses on the exports of Indian produce. There is a danger of India's balance of trade turning against her and so checking her prosperity. And it should be remembered that between 100 and 200 millions of people live on the brink of starvation, and a great permanent change in the rate of exchange must ultimately bring intense distress to millions of the helpless masses. A fixed high level of exchange must also cause enormous losses in the rupee value of the invested reserves in sterling securities and of gold held as part of the metallic reserves against the note issue. It will also cause a colossal loss if the sovereigns now held by the Indian public, estimated to amount to about 50,000,000, have to be redeemed at the statutory rate of 15 rupees to the sovereign.

11. In my opinion the gold exchange standard as applied to India is entirely discredited as a currency system intended to meet Indian conditions. I make every allowance for the difficulties with which it had to contend during and since the war, but the raising of the rate of exchange after the war was wholly unnecessary. The people of India have strong objections to the purchase of silver at the present inflated and thoroughly artificial price.

REMEDIES.

12. I discuss in detail below these and other points referred to the Committee, and now state here the recommendations I desire to make:—

(a) The money standard in India should remain unaltered; that is, the standard of the sovereign and gold mohurs with rupees related thereto at the ratio of 15 to 1.

(b) Free and unfettered imports and exports by the public of gold bullion and gold coins.

(c) Free and unfettered imports and exports by the public of silver bullion and silver coins.

(d) The gold mint at Bombay to be continued and to receive gold bullion from the public and to coin free of charge gold mohurs of the same exact weight and fineness as the sovereign and to hand them over to the tenderers of gold bullion in less than 15 days.

(e) The Bombay mint to undertake refining of raw gold for the public and not to make any profit on the transaction.

(f) The existing silver rupees of 165 grains of fine silver at present in circulation to continue full legal tender.

(g) As long as the price of silver in New York is over 92 cents, Government should not manufacture silver rupees containing 165 grains fine silver.

(h) As long as the price of silver is over 92 cents Government should coin 2 rupee silver coins of reduced fineness compared with that of the present silver rupee and the same to be unlimited legal tender.

(i) Government to coin a new 8-anna silver piece of reduced fineness and the same to be unlimited legal tender.

(j) Government not to coin an 8-anna nickel piece.

(k) Government to sell Council bills by competitive tenders for the amount defined in the Budget as required to be remitted to the Secretary of State. The Budget estimate to show under separate headings the amount of Council bills drawn for Home Charges, for Capital Outlay and Discharge of Debt. Council bills to be sold for Government requirements only and not for trade purposes, except for the pur-

pose mentioned in the next succeeding recommendation.

(l) "Reverse" drafts on London to be sold only at 1s. 3 29-32d. The proceeds of "Reverse" drafts to be kept apart from all other Government funds and not to be utilised for any purpose except to meet drafts drawn by the Secretary of State at a rate not below s. 4 3-32d. per rupee.

(m) Currency notes should be printed in India.

(n) Government not to interfere with the immemorial practice of the Indian public of melting currency coins.

(o) The sterling investments held against the Indian note issue to be liquidated as early as possible and transmitted to India in gold.

(p) The use of one rupee currency notes to be discontinued as early as possible and meanwhile not to be forced into circulation.

13. The Terms of Reference to the Committee were as follows:—

"To examine the effect of the war on the Indian exchange and currency system and practice and upon the position of the Indian note issue, and to consider whether in the light of this experience and of possible future variations in the price of silver, modifications of system or practice may be required, to make recommendations as to such modifications, and generally as to the policy that should be pursued with a view to meeting the requirements of trade, to maintain a satisfactory monetary circulation, and to ensuring a stable gold exchange standard."

Rupees and the Sovereign.

14. The outstanding effect on the Indian exchange and currency system has been that the system has broken down at a time when India enjoyed a large measure of prosperity as displayed by the foreign trade returns. The undertaking by the authorities to supply rupees without limit of amount at the rate of fifteen to the sovereign could not be maintained owing to the rise in the price of silver which made it impossible to supply fresh rupees (containing 165 grains of fine silver) at that ratio without loss. In consequence of this rise in the price of silver the standard ratio of rupees to the sovereign was given up, the sterling rate of exchange for the rupee was raised by stages to 2s. 4d., and the Secretary of State for India is now selling rupee bills at that rate which makes the present relationship of the rupee to the sovereign in working practice 11 to 1.

15. It is true that the main object which the authorities kept before themselves in working the system was to maintain the exchange value of the token rupee in meeting foreign payments. In the words of the Chamberlain Commission the "cardinal feature" of the system was "absolute security for the convertibility into sterling of so much of the internal currency as may at any moment be required for the settlement of India's *external* obligations." But whatever object the authorities had in view in working the system, this cannot alter the fundamental fact that the Indian currency was founded on the sovereign (a full value gold coin) as the money standard with rupees (token silver coins) definitely related to the sovereign at the rate of 15 to 1, and if it is impossible to maintain this ratio between the sovereign and rupees I consider that the system has failed in its most important part.

16. In support of this opinion it is necessary to recall the alterations made in the Indian currency arrangements in 1893. Up to that time India had a silver standard with mints open to the free coinage of silver. The mints were then closed and the silver standard was given up. The silver standard was replaced a few years later by the standard of the sovereign, sovereigns and half-sovereigns being made legal tender for 15 and 7½ rupees respectively, rupees being thus definitely connected with the sovereign at the ratio of 15 to 1 and also remaining full legal tender.

THE MONEY STANDARD.

17. There has been a difference of opinion as to the effect of these alterations in the currency arrangements. According to information placed before the Committee they have sometimes been described as having placed India on a gold standard, while, on the other hand, some authorities prefer to describe the Indian standard of value as a gold exchange standard since the effectiveness of the arrangements largely depended in practice on the action of the Secretary of State and the Government of India in selling or exchanging rupees for gold or sterling and sterling for rupees. But whether the standard is called a gold standard or a gold exchange standard, the alterations referred to could have no meaning except on the hypothesis that the money standard had been changed from a silver standard to the standard of the sovereign and that rupees were in effect made a fixed fraction of the sove-

reign. I cannot conceive that the mere title by which the standard is described, or any mere arrangements followed in working practice, can admit of any alteration of the ratio legally established between the rupee and the sovereign.

18. It seems to me to be impossible to exaggerate the importance of the legal standard for money payments. This standard should be and usually is regarded as less open to repeal or modification than perhaps any other legislative Act. It gives the people rights as to the kind of money they may demand in exchange for their labour or goods, rights which cannot be removed or modified without inflicting widespread injury and risking the greatest discontent. The Indian money standard was definitely changed from silver to gold so recently as 1893 for reasons affecting directly the Government of India and the Indian people, and proved to be of great benefit to India as a whole. But it is impossible to contemplate another permanent change in the rupee value of the sovereign for reasons which have not originated in India and at a time when neither the Government (apart from the part they play in the currency policy) nor the public have been inconvenienced by the standard legally established.

19. It is true that under the stress of war it has been a common expedient of Governments concerned to treat their money standards as of litte account and to resort to inflation of currency as a means of conducting the finance of war. No such reason applies to the Indian case. The inflation of the Indian currency during the war was a genuine inflation as distinguished from the artificial inflation witnessed in most of the belligerent countries. It arose from the balance of indebtedness due to India. The breakdown of the system was not due to war expenditure by the Government of India. It was caused by the acceptance in London of payments due to India in the form of sterling, which could not be transmitted to India by the usual methods. The commitments to India of the belligerent nations, as to other countries, could be met in the usual manner through exchange operations or specie remittances. They were, in fact, unable to pay in international money, and obviously the best course to follow was that in fact followed in settling similar commitments in the United States by the flotation of loans.

BRITISH LOANS.

20. Unfortunately, India had not been prepared financially for absorbing her favourable trade balances in any other form than the precious metals. Although India is normally a creditor country with trade balances running highly favourable to her, other means of adjusting favourable balances than the precious metals have not been actively sought for. That is one of the disadvantages of currency arrangements conducted by the Government. Great Britain as a creditor country set an excellent example of cancelling her favourable balances by investments abroad. There has been no encouragement in India of that method of settling trade balances. There is far more British and other money invested in India than Indian money invested abroad. Still, there is little room for doubt that, during the war, British Government loans could have been successfully floated in India on a very large scale on the same lines, and terms as some of those publicly floated in the United States to meet the expenditure of the Imperial Government. It is also probable that something could have been done to encourage Indian investors to buy the Indian sterling loans held in London, if arrangements had been made for payment of the interest at the Government district treasuries in India.

21. The break in the standard ratio during the war was, however, less serious than the still greater break during the present year. The overwhelming demands for war requirements were at an end, and, although trade demands were urgent, it was imperative, in the interests of the great majority of the people of India, that their rights in the standard money of the country should have been protected from further modification. Trade and circumstances, especially in peace, must conform to the standard of money rather than that the money standard should accommodate itself to them. If it was impossible to meet trade demands without breaking the standard, that would be a reason for declining to meet them, but hardly a reason for meeting them and breaking the standard.

II.—Watering the Note Issue.

22. With regard to the note issue there has been a complete reversal of the procedure formerly observed in the matter of the fiduciary issue the effect of which on the note issue itself can only be described as extremely unfortunate. The former practice was to increase the fiduciary issue by investment of a portion of the metallic reserves, and this was done only when the proportion of the latter to the total of the notes in active circulation had shown, over a considerable period, a position sufficiently

strong to warrant an extension of the invested reserves and a corresponding diminution of the metal reserves. During the war, however, the fiduciary issue was expanded to an enormous extent without regard for the considerations which formerly decided extensions of that form of issue. It was no longer a case of investing a portion of the metallic reserves held in India against outstanding notes; notes were boldly issued against which no metallic reserves in India had ever existed. Also the proportion of the metallic reserves to the total of the outstanding notes was not allowed to have any weight. It was a case of simply watering the note issue in its worse form—issuing notes without any metallic backing. In other words, it was a forced loan from the Indian public free of interest. It was an extreme measure to apply to the Indian note issue even during the war and at a time when there were immense sums held in London belonging to the Indian currency. Indeed, it appears to have been adopted because of the difficulty of transferring the balances held in London to India. But even so, the warnings which had been given at the outbreak of the war, when there was a run on the paper currency offices for the encashment of notes, should have shown the necessity of maintaining the note issue in a strong position and the undesirability of weakening it by an overissue of notes.

23. No exception can, of course, be taken to the security held against the notes thus issued which consisted of British Treasury bills, but the better course would have been to invite the public to take up the bills or some other form of British securities. The public might not have cared to accept the same rate of interest as the India Office obtained on the investments, but even if it had been necessary to pay a higher rate of interest it would have been better to face this cost rather than imperil the safety of the note issue.

INCONVERTIBILITY.

24. Not unnaturally there was much discussion as to the note issue becoming an inconvertible issue, and, indeed, an actual state of inconvertibility was only avoided by the narrowest of margins. To my mind inconvertibility would be a disaster of the first magnitude for the note issue and for India. It would destroy all confidence in Government's own paper money. Not only so but, seeing that British Government securities are so largely held against the note issue (the amount is Rs. 835,000,000 which, at the present rate of exchange of 2s. 4d., is approximately 93,000,000l.), the credit of Great Britain is also involved.

25. I have mentioned that an actual state of inconvertibillity was avoided only by the narrowest of margins. This was aided by the exceptional measures taken restricting the movement of coin by rail and steamer, which had the effect of confining exchange ability of notes into coin to the seven head currency offices. Even now in these offices conversion of notes into coin is directly and indirectly impeded.

26. Nothing can better show the effect on the public mind of the great expansion in the fiduciary issue and the methods adopted to avoid demands for encashment than the fact that currency notes were quoted at a heavy discount. A telegram from the Viceroy, dated the 8th November, 1919, stated that the highest rates of discount on currency notes reported during 1918 were 19 per cent. in the Central Provinces, 15 per cent. in Bengal, 13¾ per cent. in Burmah, but His Excellency added that during 1919 the highest rate reported was 3 per cent. This telegram showed not only a very high rate of discount in 1918, but also that it was widely spread throughout the country, and while it is satisfactory that the rate of discount has fallen to a low figure this year the fact that such a considerable discount existed is one that must have a lasting influence on the minds of the public. The Governor of the Bank of England, in the course of his evidence before the Committee, remarked that a premium on gold was a very vicious thing. I think that, in the sense that a premium on gold is vicious, a discount on currency notes within India is equally vicious.

METAL RESERVES.

27. In view of the great disturbance to the credit of the paper currency arising from the great expansion of the fiduciary issue, I consider that the metal reserves should be strengthened as early as possible by the liquidation of the reserves invested in London, and also that, in order to reestablish confidence, a high percentage of cash reserves should be maintained for many years to come. About 80 per cent. would not be too high a figure to fix as a normal proportion of metallic reserves to the total of notes outstanding. It must be remembered that this metallic proportion on the 31st March of each year from 1910 to 1915 inclusive averaged 78.2 per cent.

28. A well-conducted note issue is not only an economical and therefore profitable form of money, but also has an important educative effect in a country like India with a backward and ignorant mass of people. Also, it should be remembered that

the internal trade of India is much larger than the external trade. Mr. E. M. Cook, C.I.E., of the Finance Department, has expressed the opinion that the internal trade is certainly fifteen times larger than the external trade, and that possibly the proportion is even higher. The ultimate possibilities of extending the note issue are therefore very great, but the first essential is to ensure that there shall be no grounds for distrust of the issue, and particularly that nothing should be done to give cause for the notes to pass at a discount.

III.—The Price of Silver.

29. The Committee were also asked to consider the bearing of possible future variations in the price of silver on the currency system and practice. The reference of this question to the Committee shows the great importance attached by the authorities to the continued use of silver in settling India's trade balances, even although the use of silver cannot be continued for the present without breaking the standard ratio. It is, in fact, the crux of the whole situation.

30. Information placed before the Committee lays great stress on the effect of the Pittman Act in the United States in its reaction on the price of silver and on the Indian currency position, and it was the high price of silver which was the reason given for raising the rate of exchange during recent months which had the effect of altering the standard ratio between rupees and sovereign.

31. It is almost impossible to exaggerate the effect on the silver market of the raising of the rate of exchange for the rupee and making the rate more or less closely dependent on the price of silver on the ground that that price made the rupee more valuable as bullion than as a coin if the rate was not altered. It excited and inflamed the silver markets with anticipations of continued buying on account of the Indian currency at rising prices and there are not wanting signs that silver interests are prepared to take full advantage of the situation created by this measure.

RISE IN SILVER.

32. I am unable to fall in with the idea that the rise in the price of silver afforded solid ground for this recent great alteration in India's money standard. On the contrary, I contend that the price of silver has been artificially forced to its high level by the exclusion of stocks of Indian silver from the world's markets by means of the continuance of the prohibition of exports of silver, and the raising of the exchange rate. The position is that the American production of silver is shut out of the world's market automatically by the operation of the Pittman Act if the price of silver should fall below 1 dollar per fine ounce. The Act requires that until the silver taken from the dollar reserves is restored, the United States Treasury must buy at 1 dollar per fine ounce any silver of American origin tendered to it at that rate. This provision in the Pittman Act has been taken as establishing in effect 1 dollar per fine ounce as the minimum price of silver until the amount of silver withdrawn from the dollar balances has been restored, and since the silver dollars withdrawn under the Pittman Act for the Orient represent between twice and three times the normal American production, it is estimated that the process of restoration will extend over a period of several years. The future production of American silver being thus assured of a market at a stated price, owing principally to the demands for Indian coinage during the war, and the current of trade showing the probability of fresh demands for India, while China was a keen buyer it was only to be expected that the price of silver would rise. At the moment of writing the price in London is about 78d. This price has been made possible only by the prohibition of exports of silver from India and by the raising of the rate of exchange, which has the effect of lowering the rupee value of all silver held there and making exports unprofitable. But for the prohibitory orders and the raising of the rate of exchange it would have been profitable for Indian holders to sell silver, and Indian sales would have prevented the great rise in price which has taken place. Under these circumstances, the high world price of silver can only be regarded as wholly artificial, and consequently as a reason for such a drastic step as the alteration of the money standard ratio between rupees and the sovereign has no weight.

33. It is frequently said that India is a sink for the precious metals and never allows them to come out. Here was an opportunity of disproving such statements. Silver would have been freely exported but for the measures taken by Government to prevent exports.

INDIA AND SILVER.

34. The exclusion of India's silver from the world's market is not altogether a new thing. It was practically excluded by imposing a duty on silver imports and not refunding the full duty paid when the silver was re-exported, and granting no refund of duty whatsoever on melted silver ornaments coming from the districts even in time of famine. I add a note on this subject in the ancillary problems dealt with at the end of this report.

35. There is the objection that it was necessary to protect the silver currency against depletion by export by means of ordinances forbidding exports. This is an objection which would have very great force in a country like the United Kingdom where the subordinate silver currency forms a small percentage of the total amount of all kinds of currency in active circulation the loss of which by export would cause the greatest inconvenience. In India it has very little force because the total amount of silver currency is far in excess of the quantity in active circulation and held against the note issue. It is estimated that there are about 3,000,000,000 to 4,000,000,000 of rupees in India. Moreover the amount that India could sell for export could not have reached very important dimensions because foreign buying power is limited, while Indian silver would not be accepted by the United States Treasury to replace the dollar balances since the replacement has to be made from silver of American origin.

36. A more serious objection to permitting silver exports was the extreme vulnerability of the paper currency reserves of coin, because of the extent to which the note issue had been watered by ordinances sanctioning the issue of notes in India against British Treasury Bills held in London. But here again the position was most artificial. The expansion of the note issue on the security of British Treasury Bills was in effect a forced loan from the Indian people, a method of meeting the difficulties of the time which I venture to suggest should not have been resorted to. The proper course was to suggest to the British Treasury the desirability of floating public loans in India on the lines of those raised by the British Government in the United States, if the payments to India in London could not be completed by transmission to India in the usual manner.

SELLING CURRENCY.

37. A real practical difficulty in the way of removing the embargo on silver exports as contrasted with the difficulty artificially created by the watering of the paper currency, was that silver exports would have increased the amount of the balance due to India, which the authorities were already unable to transmit to India, and would also have involved a change in the method of adjusting the balances. Obviously, with silver exports, it would have been absurd to continue to settle the trade balances by means of the sale of rupee bills in London. The settlement would have had to be made in gold or by some form of deferred payments. The latter form of adjustment would not have been easy in the absence of preparation of the Indian market to take outside securities. And there would, no doubt, have been the usual objections to India being paid in gold. Still, I venture to think that even if gold had been required India could reasonably have expected consideration in the special circumstances of the case, especially after the war was over, and the embargo on gold exports had been removed in the principal money centres. The point at issue was a vital one for India, namely, whether India should be compelled to give up a vital part of her established money standard because the price of silver had made her token silver currency more valuable as metal than as coin. India had the power, and it would have been profitable for her and to her interest to prevent the rise in the price of silver by sales of the metal. The mere fact of Indian sales would have broken the strength of the silver market. In such circumstances it would not have been unreasonable for India to ask that her trade balances should be paid in gold so that she should be able to export silver for the preservation of her money standard.

38. Since the above was written it has been reported that the United States Government have followed the method here suggested by offering to sell silver currency when the price of silver went above the melting value of their silver coinage. It seems to me that what is being done in America could have been done in India.

THE STANDARD RATIO.

39. But even if exports of silver were not allowed for the purpose of preventing the price of silver from rising, there was still no occasion to adopt the extreme measure of raising the rate of exchange, and so breaking the standard ratio. India did not require additional supplies of rupees. She could carry on for many years without any new silver coinage. The only alteration required would have been to stop the

coinage of rupees, and that would have occurred automatically by reason of the loss coinage would involve. But if the coinage of silver ceased because it was unprofitable, the trade balances if they continued to be favourable would have to be settled by other means than importing silver. It appears to me that the authorities were not willing to permit of a settlement by other means. They had come to regard the practice of selling rupee bills in London without limit of amount as an all essential part of their duties in the administration of the currency which could not be given up. Yet the position proved that there was in fact a limit to the issue of rupees if the standard ratio was to be maintained, since rupees could no longer be coined without loss at that ratio. Rather than give up the sale of rupee bills the authorities raised the rate of exchange, so breaking the ratio, and continued to offer rupee bills for sale.

40. Still another method of avoiding the raising of the rate of exchange because of the high price of silver would have been to impose a duty on all exports at a rate sufficiently high to provide the means of meeting the additional cost of silver over the price at which silver could be bought and coined without loss at the fixed ratio. Such a duty would have the effect of moderating the foreign demand for Indian produce, and thereby moderating the balance of trade due to India; while on the other hand, if India is compelled to accept payment in silver, the duty would enable India to avoid paying more for it than the price at which it could be bought and coined without loss.

41. The authorities considered that there were only two alternatives open to them, either to raise the rate of exchange or to debase the silver coinage. I have endeavoured to show that there were other courses open to them without raising the exchange or debasing the rupee coins. But even if it were the case that they had only these two alternatives it is by no means certain that they took the better of the two. My own belief is that the people of India would prefer debased silver coins to an alteration of the ratio which the raising of the exchange involves. It would not be practicable or advisable to call in all the rupees in the hands of the public to be recoined, but any new coinage that became necessary could be issued in the form of a special silver coin, such as, for example, a two-rupee coin containing a reduced quantity of silver.

EXCHANGE AND SILVER.

42. In connection with the question of debased coins I may say here, by way of parenthesis, that although the Government of India have taken power to issue a nickel half rupee or eight anna coin I trust that they will hesitate before putting it into circulation, and also that the suggestion which has been made that the eight anna nickel piece should be made legal tender for a larger amount than one rupee will not be agreed to. The appearance in the currency system of one rupee paper notes and of two anna nickel coins has sufficiently alarmed the Indian people and led to the hoarding of rupees. It is unsafe to carry the debasement of the coinage any further by the use of nickel coins. I am of opinion that the eight anna nickel piece should not be put into circulation at all, and I suggest that instead of it an eight anna silver piece of reduced fineness should be coined and made unlimited legal tender, the existing eight anna coins being withdrawn from circulation for recoinage at the reduced fineness. The practice of issuing subordinate coins of reduced fineness has been followed in the coinage of France and of the United States, and it seems to me much preferable to the use of nickel for such a high valued coin as the eight anna piece in India.

43. The authorities in raising the rate of exchange were, no doubt, influenced by the difficulties there would have been in settling the balance of trade by other means than silver, and especially gold. But I venture to question whether they have the right, by executive action, to disturb the legally established money system. The people of India are accustomed to complaints from financial quarters about India's absorption of gold, but they were fairly entitled to expect that their rights in the money standard would have been protected so far as the Government authorities were concerned.

44. Also, it is difficult to see where the advantage lies, in making the rate of exchange follow the price of silver. If silver has to be bought at present prices and coined into rupees at the present rate of exchange there is no economy of any consequence in using silver instead of gold. One of the advantages claimed in former years for issuing rupees instead of sovereigns was that it was economical. The rise in the price of silver took away that advantage.

INDIA AND GOLD.

45. I deal later with some of the objections raised to Indian demands for gold, but here I may point out that there is

some misapprehension on the subject. The foreign trade of India is normally conducted with 77 other countries. From the following statement which I had supplied to the Indian press it will be seen that in the year 1913-14 (which was the last normal year before the war) the trade with each country resulted in a balance against India in the case of only five principal countries, the total adverse balance being 47,807,900l., of which the principal one, the United Kingdom, had a balance due by India of 40,098,800l. All the other countries trading with India had to pay over 88,462,300l. to India. When, therefore, India takes gold it is because gold as the international form of money is due to her in payment of commodities supplied to those other countries.

Countries.	Exports of Merchandise from India.	Imports of Merchandise into India.	Balance of Trade against India.	Balance of Trade in favour of India.
	£	£	£	£
United Kingdom ..	38,234,300	78,333,100	40,098,800	..
Java, Borneo and Sumatra ..	1,415,500	7,773,900	6,358,400	..
Mauritius and Dependencies ..	867,700	1,685,100	817,400	..
Norway and Sweden ..	..	497,400	497,400	..
Persia ..	438,800	474,700	35,900	..
Japan ..	15,124,500	3,187,700	..	11,936,700
United States of America ..	14,518,100	3,186,100	..	11,332,000
France ..	11,711,500	1,794,900	..	9,916,600
Germany ..	16,867,500	8,452,000	..	8,415,800
Ceylon ..	5,866,300	548,100	..	5,318,200
Belgium ..	8,008,400	2,839,000	..	5,169,400
Hong Kong ..	5,102,300	654,900	..	4,447,400
Italy ..	5,219,000	1,478,100	..	3,740,900
Austria-Hungary ..	6,408,800	2,844,800	..	3,564,000
South America ..	3,181,800	800	..	3,181,000
Egypt ..	3,202,700	199,700	..	3,003,000
Australasia and Oceania ..	3,321,500	651,600	..	2,669,900
China Treaty Ports ..	3,799,200	1,136,700	..	2,662,500
Straits Settlements ..	4,367,500	2,293,200	..	2,074,300
Russia ..	1,636,200	37,700	..	1,598,500
Spain ..	1,479,200	..	..	1,479,200
Turkey in Asia ..	1,782,900	379,200	..	1,403,700
Holland ..	2,359,700	1,033,400	..	1,326,300
Canada ..	952,000	..	..	952,000
West Indies ..	561,900	..	..	561,900
Natal ..	535,100	..	..	535,100
Aden Dependencies ..	816,200	286,700	..	529,500
Indo-China ..	509,400	..	..	509,400
East African Ports ..	342,000	66,600	..	475,400
Siam ..	621,900	185,300	..	436,600
Arabia ..	796,400	383,100	..	413,300
British East Africa ..	506,000	258,900	..	247,100
Cape Colony ..	243,700	..	..	243,700
Portuguese East Africa ..	331,100	100,500	..	230,600
Turkey in Europe ..	70,800	..	..	70,800
Other Countries ..	1,421,400	1,403,900	..	17,500
Total ..	162,821,500	122,167,100	47,807,900	88,462,300

IV.—The Requirements of Trade.

The Committee were further asked to make, recommendations as to the policy that should be pursued with a view to meeting the requirements of trade and to maintaining a satisfactory monetary circulation. It is very easy to exaggerate the importance of meeting the requirements of trade. Trade elsewhere is accustomed to finding its requirements met without the active intervention of Governments by means of sales of Government bills. The usual and correct attitude of Governments is to provide machinery for coinage and to leave it to its own automatic action, except for the provision of subsidiary coins. There seems to be no good reason for trade with India to be conducted on different lines from those followed by other advanced countries. The requirements of trade in this connection consist of finding the means of exchanging foreign money for Indian goods to satisfy the needs of the moment. Trade as such is not concerned with currency policy or with the economic effect produced by the method of carrying out its exchanges. Its concern is purely personal and temporary to see each transaction completed. The concern of the Government, on the other hand, should be to protect and safeguard the interests of the people as a whole in the maintenance of the legally settled standard, and I consider that Government would be performing its duty better by paying more attention to this aspect of the question than by showing anxiety for trade requirements. It is no doubt a convenience for banks and some of the public to be able to get Government rupee bills for making remittances to India, and, when required, also from India. But it is not a convenience that trade has any right to look for. So far as the Secretary of State has to sell bills to meet Government's own requirements, the practice of offering the bills for sale is unobjectionable. But that is not the case when bills are sold in excess of Government's own needs and without limit of amount on the ground that such sales meet trade requirements. The real reason for this latter practice is not so much to meet the convenience of trade as to retain the power of diverting payments of India's foreign balances from gold to silver.

V.—The Gold Exchange Standard.

47. The Committee were further asked to make recommendations as to the policy which should be pursued with a view to ensuring a stable gold exchange standard.

48. Before examining the working of the exchange standard I think it desirable to refer to some of the objections raised to the Indian money system.

49. The Governor of the Bank of England in the very important evidence he gave before the Committee, while he disclaimed any knowledge of Indian conditions, commented freely on the money methods practised in India. This criticism, coming from the highest currency authority in England, calls for careful consideration. A few of what appear to me to be his principal ojections may be stated.

50. He took exception to the medium of exchange (gold) being used as a vehicle for hoarding instead of being left to play its part in the regulation of the exchanges. It was a wasteful employment of gold and detrimental to the interests of the individuals who practised it and to those of India as a whole. He thought it would be much more to the interests of India as a whole that her favourable trade balances should be invested in some productive form abroad, as Great Britain used to settle her favourable balances by investing them in foreign interest-bearing securities. He also thought the Imperial Government would have some grounds for imposing restrictions upon the unlimited demand of India for gold in satisfaction of the balance of trade, and also because India had managed with reduced supplies of gold during the war he thought she ought to be able to continue to do so. For internal circulation notes, he said, were as good as gold, as the experience during the war had proved in England, and all the gold that was required was the amount likely to be withdrawn for export by presenting notes.

51. From these opinions it is clear that the Governor of the Bank thinks that India should economise the use of gold on the same lines as those followed in England. This is not the place to discuss the merits and demerits of the English system, but since it is put forward as an example for India to follow it seems necessary to say that, so far as the economy of gold in the internal circulation is concerned, the greatest agency in securing it has been the deposit-cheque system which originated with the bankers and their customers, apart from, and it is sometimes said in spite of, the Government of legal system of currency. Also, the methods by which the internal economy of gold for circulation purposes was attained in England developed simultaneously with the growth of the method of cancelling or avoiding gold imports in settlement of favourable foreign exchanges by means of foreign investments.

HOARDING.

52. With regard to the suitability of this system for India it seems necessary also to draw attention to the psychological difference between the people of India and the people of England. The people of India are a subject people with a history of many centuries behind them of insecurity of private property. They have been driven by the force of circumstances in the past to secret as far as possible such property as they valued. The British people, on the other hand, have a long, proud record of insular security. They are an independent race, and their enterprise has carried them all over the world, where they have formed connections and found favourable investments to the great advantage of individuals and of their mother-country. If, therefore, the British people have themselves, independently of their Government been successful in developing currency measures which have economised gold so satisfactorily to themselves this must very largely be attributed to their national characteristics and their historical sense of security. It cannot necessarily follow that the same gold economising measures are suitable to India, where the people have different traditions.

53. So far as the objectionable hoarding of gold is concerned there is not only the old tradition of insecurity of property inducing them to hoard, but there is the comparatively new form of internal token currency, not exchangeable into gold, which makes a very strong additional inducement to those who can afford it to hoard gold for security, as explained in a later paragraph.

54. In the matter of internal currency, India has nevertheless made considerable progress in the direction of following English currency methods, particularly in the form of notes and cheques, although she is a long way from economising to the same extent as in England in the metallic backing to cheques.

LARGER LOANS.

55. But while India still requires, and must require for a long time to come, a very solid metallic backing for her credit currency, that is not to say that she requires constant additions to her metallic currency merely because her trade balances are favourable. When the Governor of the Bank of England suggested that India should follow the English practice of settling favourable foreign balances by investments abroad, he touched the weakest spot in the administration of the Indian currency system, and pointed the way to the real remedy to avoid excessive demands for the precious metals and particularly gold. The

policy has been to sell rupee bills on India in London without limit of amount, which meant to any extent that might be necessary to settle the trade balances, and while the policy did not exclude Indian investments abroad, it left the matter to individual initiative, and did nothing to favour or encourage such investments. Yet, if the objections raised to the absorption of the precious metals in adjustment of trade balances are to be satisfactorily met, it can only be by means of investments abroad by India, or, which is very much the same thing, by other countries borrowing in India.

56. The war afforded a favourable opportunity for getting India into the way of absorbing favourable trade balances by lending to Great Britain, an opportunity of which advantage was not taken. It may be said that India had some difficulty in raising the loan of 100 millions which she voluntarily contributed to the cost of the war. There was not the same inducement in that case, that there would have been in the case of a loan offered by the British Government, and the rate of interest offered was not so good as the interest paid in some cases for similar public loans raised elsewhere by the Imperial Government. India is full of money, and notwithstanding the general idea that it is not available for investment, in my opinion it is a question of terms and security.

57. Since the wide break in the standard ratio between rupees and the sovereign with its attendant unsettlement and feeling of insecurity, there is now less chance of India seeking investments abroad than ever. There are in addition to the instability and insecurity of the money standard, questions connected with foreign investments which must scare Indian capital, such questions, for example, as foreign taxation, capital levies, and inflated values due to artificially inflated currencies. But the same results, so far as the settlement of exchanges are concerned, could be obtained by the raising of foreign and particularly British loans in India.

58. Under the present system it can no doubt be claimed that India does in fact lend abroad through the investments held against the paper currency issue. But in so far as such investments represent either a forced loan from the people of India free of interest, or a tax on the money of the Indian people as explained later, they are not free of objections. I hardly think the Governor of the Bank had such loans in view when he made his suggestion as to India investing abroad.

GOLD EXCHANGE STANDARD.

59. Coming now to the working of the gold exchange standard, it seems necessary to mention the fact that the Indian money standard has been the subject of constant public controversy for many years. I have already referred to the difference of opinion as to whether it was a gold standard or a gold exchange standard. But the mere fact that there is any opening for this controversy is, by itself, a most undesirable and unsettling feature in money affairs. The standard should be so fixed and defined as to leave no possibility of dispute or question as to what it really is. As already stated, I take the view that the legally established money standard is the sovereign with rupees definitely related to the sovereign at the rate of 15 to 1.

60. In contradistinction to this legally-established standard, the gold exchange standard has no legal validity. It has not been clearly and explicitly defined. The authorities who conduct it exercise the widest discretion in its regulation, but hitherto have been careful to respect the legally-constituted ratio between rupees and the sovereign. Its usual working characteristics are well known. In one direction the object aimed at is to provide absolute security for the convertibility into sterling of so much of the internal currency as may be required for the settlement of India's external obligations. In the opposite direction it undertakes to sell rupee bills on India without limit of amount. In aiming at the maintenance of the sterling exchange it resembles the English system which, before the war, made a point of seeing that the exchanges remained within the gold points. In undertaking to sell rupee bills on India without limit the gold exchange standard system is unlike the English model, which, by means of the Bank rate, restricted expansion in the volume of internal credit currency and made it dependent upon the extent of the gold reserves.

61. The undertaking to provide rupees, which are token coins, without limit of amount, may in one sense be considered as authorised by the circumstance that rupees equally with sovereigns and half-sovereigns are full legal tender. Under the old silver standard rupees were, of course, legal tender, and when the standard was altered it was necessary to continue them as legal tender because of the great quantity which was then in circulation. But whether, from the point of view of the statutory standard of the sovereign, the tremendous volume of rupees which has

been added to the token currency can be justified is another matter. In reality the endless issue of token coins, much in excess of what is needed for internal exchange purposes, amounts to a form of taxation on the money of the public. It is this circumstance that is to a very large extent responsible for the extraordinary demands for gold and sovereigns in India. It virtually compels the Indian people to seek full value for the token money with which they have been over-supplied for ordinary currency purposes, and is thus largely responsible for the hoarding of gold of which so much is heard. India's hidden stores of gold can never be expected to be used profitably for the benefit of the holders or of the State so long as no reasonable assurance is provided that, when used, they will remain a gold asset, and that assurance is not provided by a currency in circulation entirely composed of or based upon token coins.

62. When I say that the issue of rupees largely in excess of what is needed for ordinary internal exchanges constitutes a form of taxation on the money of the public, it is necessary to add that the difference between the cost of gold coins and silver coins, which is the amount of the tax, does not go into the Indian Treasury balances, but goes to form gold or invested reserves in London which are intended to meet remittances from India at a fixed rate which cannot be made so advantageously through other channels. But even if the profits on coinage went to swell the revenues of the Government they would be no less open to the very serious objection that they really formed a tax on the money of the public.

63. In present circumstances, however, this form of taxation has practically ceased, since the coinage of rupees at the moment is not profitable. But as a counter-balance to the virtual disappearance of this tax, the latest development of the gold exchange standard system has, by raising the rate of exchange and breaking away from the statutory standard ratio, depreciated the commercial value in rupees of the whole of the rupee currency which has already been taxed.

DEBTORS AND CREDITORS.

64. This latest development gives ground for the gravest anxiety, not only on account of the depreciation in value of the immense volume of the rupee currency, but also because it means a revolution in the financial and economic life of India.

65. It alters as it were by a stroke of the pen, the existing relations between creditors and debtors. It cuts down the value in rupees of all existing holdings of the precious metals in India relatively to their value in the markets of the world, including the gold portion of the reserves held against the note issue, and, similarly, it cuts down the value in rupees of all existing and future stocks of Indian produce, and through this effect on the value of produce it is bound to prejudicially affect scores of millions of Indians engaged in agriculture, whose struggle for existence is already most severe. It is not too much to say that it will threaten the very existence of millions of such people. It will further handicap Indian industries in competition with similar industries abroad and will severely check the prosperity of India. No doubt there will be some compensation. The finance of the Government will be relieved so long as the rate of exchange remains high, since the home remittances will cost considerably less in rupees, and it will be an advantage to those who buy imported goods or have payments to make outside of India.

66. It has been urged that one beneficial consequence will be the lowering of the high price level in India. This may be granted, since the value in rupees of Indian produce, the price of which is ruled by outside markets, must fall. But it is nevertheless a questionable method of reducing prices. There has been no artificial inflation of the currency. Inflation of the currency has been a genuine inflation in India caused by a surplus of sales over purchases abroad. Even the forced loan in the paper currency issue is represented by debts due by the British Government. By the change in the standard ratio prices will be brought down, since prices are reckoned in rupees; but there is not the same good reason for changing the standard money to reduce prices that there is for deflating an artificially inflated currency to obtain the same result. In my opinion the inflation of currency in India is the consequence rather than the cause of high prices. The currency has been inflated because the balance of trade was favourable and because additions to the currency were the normal way of settling trade balances. The balance of trade was increased by the increased prices paid for commodities for export. In this way the additions to the currency were a consequence of high prices. On the other hand, the inflation of currency cannot in its turn be held to have raised prices, since all accounts go to show that currency of all

kinds has been hoarded on a very large scale, and hoarded money does not act on prices. The change in the standard ratio will bring down rupee prices, but it will leave undisturbed the real cause of the high prices in India, which was that world prices were high and world prices were high mainly because the currencies of many countries were artificially inflated. It is simply a case of altering the nature of the money in which prices are reckoned, and, when advanced in excuse for the change of ratio, can only be regarded as an argument to deceive the people.

BALANCE OF TRADE.

67. The effect of the change outside of India cannot be so clearly estimated. But the probabilities are that with the higher sterling cost of the rupee the demand for Indian produce will fall off, while remittances from India being cheaper in rupees imports will be stimulated. If these probabilities should materialise India's trade balances will become less favourable to her than they have been, or it may be the trade balances will turn against her. In either event the London market, where India's international trade is mostly financed and finally adjusted, will be relieved of the necessity of settling India's trade balances by means of specie remittances to the same extent as formerly, if indeed specie remittances to India will be necessary at all, while in addition to that advantage the stimulation of imports by the reduced rupee cost of sterling exchange will increase the demand for English textile manufactures.

68. These revolutionary changes in the Indian money system should not have been possible and much less necessary at a time when immense sums were due to India in exchange for her commodities. They are to be explained by the particular bent of the policy followed—a policy of making India accept payment in India of the balances due to her as far as possible in the form of rupees. A policy less rigidly bent in that direction would have been susceptible to the need for meeting the very special circumstances of the time by other methods, such, for example, as that suggested by the Governor of the Bank of England when he pointed out the desirability of investments abroad in settlement of India's foreign claims. It is a policy which has persistently ignored the essential safeguards of a gold standard, and particularly the safeguard of limiting the issue of token coins. It has by mere executive action changed the legally-established gold standard into a gold exchange standard, making the maintenance of exchange the object to be attained in place of the provision of gold money with a limitation of token money. And while the maintenance of exchange was the main object, the policy has broken away from the normal rate of exchange on the ground that the rise in the price of silver rendered that course necessary, although, as I have endeavoured to show, there was no real necessity for doing so. The fact that the maintenance of exchange was so readily abandoned and the sale of rupee bills continued, combined with the persistent flooding of India with silver token money, gives ground for the theory that fixity of exchange was only the ostensible object of the policy, and that the real object was to compel India to take silver in place of gold money. Further, it is a policy which is settled and managed in London, and which necessarily operates in the markets of London and India. That the interests of the London market have not been without influence in shaping the policy may be gathered from the enormous sums of money or investments belonging to the Indian currency which have been accumulated there. The profits on silver coinage were steadily collected into the gold standard reserves in London, and now that the coinage of silver has ceased to be profitable, a new departure has been made in the issue of currency notes in India on the security of investments in London, which has had the effect of rapidly accumulating an enormously increased store of Indian currency money in London. These are changes which will be viewed in India with the gravest concern and mistrust.

69. India is fairly entitled to a system of sound money. The gold exchange standard has failed to provide such a system, and I am unable to make any recommendations for its continuance which would secure the stability it has lost. I consider that the authorities had no right to take the action of raising the rate of exchange and, in my opinion, it is their duty to proceed to undo what they have done.

VI.—Policy.

70. On the subject of policy I desire to associate myself generally with the views expressed in the following extract from the able memorandum submitted to the Committee by Sir Stanley Reed, Kt., K.B.E., LL.D., of Bombay:—

"... I am strongly of opinion that the control now exercised by the Secretary of State over the Indian exchanges should

be abolished at once. Official control over the exchanges is always a bad thing, and whilst possibly justified under the immense strain of the war, should not be retained a moment longer than is absolutely necessary. It has already been abolished in every other country in the world, and it should be abolished in the case of India with the minimum of delay. Whilst this is true as a financial proposition, it is specially true of a country in the political condition of India. The Government of India, and to no less a degree the Secretary of State, is suspect in the eyes of a large section of the Indian community. All its actions are jealously regarded, often misunderstood, no less frequently misrepresented. The Secretary of State operates 6,000 miles from the great Indian financial centres. He is surrounded by, and naturally amenable to, interests which are not Indian in their ideas and aims. He acts in secret, and it is frequently impossible to obtain any information in India of the groundwork of measures which, however, wise and expedient in themselves are not understood and are liable to perversion in India itself. The political disadvantages of such complete powers being exercised in secret so far from the people who are vitally affected by them, cannot easily be exaggerated. The only remedy is for the Secretary of State to divest himself as completely as possible from the management of the Indian currency and exchanges, and to allow these to be governed by normal conditions. It is essential, therefore, that the fixing of the exchanges by the Secretary of State and the distribution of Council bills amongst a limited circle of 'approved' buyers should not be restored. Council bills should be sold by open tender to whomsoever may apply, the only limitation being the smallest amount to be tendered, which might be retained at the figure of 10,000 rupees. Whatever inconveniences may attach to this procedure will be outweighed by the practical advantage of freeing the Secretary of State from the suspicion which, however unwarranted, is widely entertained, of subordinating the interests of India to those of financial institutions in the City of London, and of giving banks with their headquarters in London a preference over banks with their headquarters in India.

"The first of these essential steps is to remove all restrictions on the free movement of gold and silver bullion to and from India, and to establish free and unfettered trade in both precious metals. It is the inalienable right of every creditor country to determine for itself the form in which its debtors shall be paid. India is a creditor country and will remain a creditor country for as far ahead as we can see. India is a billion-using country, and the present exchange and currency difficulties have largely arisen from the arrest of the normal flow of gold to India and the substitution of credits abroad by Government for the liquidation of the large balance of trade. Deprived of the normal supply of gold bullion, India has turned to the only precious metal available, and has absorbed coined rupees in prodigious quantities. There can be no financial health in India until this traditional demand for bullion is satisfied. The Currency Commission of 1913, presided over by Mr. Austen Chamberlain, laid down that 'the extent to which India should use gold must, in our opinion, be decided solely in accordance with India's own needs and wishes, and it appears to us to be just as unjust as to force gold coins into circulation in India on the ground that such action will benefit the gold-using countries of the rest of the world, as it would be to attempt to refuse to India facilities for obtaining gold in order to prevent what adherents of the opposite school have called the drain of gold to India.' The demand for freedom of trade for India in the precious metals comes from every important financial and commercial authority in the land, and it must be boldly and unequivocably recognised.

"It is objected that India is a bottomless sink for the absorption of the precious metals, and that gold once passed into general consumption in India is permanently lost to the rest of the world. This attempt to fasten upon India an exceptional and invidious responsibility for the consumption of gold cannot be too vigorously combated. India is still an illiterate country, whose credit and banking facilities are miserably unorganised and where the practice of holding small savings in gold and silver ornaments is centuries old. Yet its normal demand for the industrial arts, and for the satisfaction of the social customs of three hundred and fifteen million people, was met before the war by about ten millions of gold annually. The United States of America was reported recently to be absorbing a million sterling in gold per month for industrial purposes. Yet no one says that the United States is a bottomless sink in the matter of her

gold absorption. It is stated that in England one of the most flourishing trades during the war was that in cheap jewellery, in which form the working classes invested a substantial proportion of their increased earnings. Every country in the world uses gold and silver for industrial and domestic purposes, and it induces a sense of angry injustice to find that the Indian demand for the precious metals, for precisely the same purposes, is perverted into senseless hoarding, especially when the history and conditions would justify a far larger gold absorption than the Western nations with their general literacy and highly organised credit systems can claim.

"The success of these and any other measures which may be adopted will largely depend on the publicity with which they are carried into effect.

"Attention has already been drawn to the particularly difficult task which the Government of India has to discharge owing to the political status of India. That political status inevitably exposes all the acts of the Government of India to distrust, misrepresentation, and prejudice. Whilst this is true of the Government of India, which is in close contact with Indian opinion, whose members are well known in all commercial and financial centres, and where successive Finance Ministers have made it a practice for a number of years to keep in personal touch with financial and commercial opinion, it is doubly true of the Secretary of State the final authority in all financial matters affecting India, who operates six thousand miles away, remote from Indian thought, feeling, and influence, but in living contact with the London market. Experience has taught us that the only remedy for misunderstanding in India is publicity; the antidote to misunderstanding and distrust is the truth. A mountain of misunderstanding of the most regrettable character, involving political dangers of great magnitude, has been reared by the secrecy with which the Secretary of State controls Indian financial policy; this mountain can be levelled only by the truth, spread with the widest publicity. It follows, then, that all financial operations carried on by the Secretary of State should be conducted in public and that the path of wisdom lies in the Secretary of State divesting himself so far as possible from the management of the Indian currency and exchanges, and substituting for this management automatic operations carried out in the gaze of the public.

"An important step in this direction will have been taken if a free, open, and automatic exchange is established, Council bills being sold to the highest tenderers. But it will be necessary to supplement this measure by others in the same direction. All purchases of silver for the Government of India should be by open tender to be delivered in Bombay. Quite apart from the fact that this will attract to the great bullion market of Bombay silver from all parts of the world, it is the only means whereby the cloud of suspicion which overhangs the purchases of silver for the Government of India can be dispersed. The returns relating to all operations—currency and exchange—undertaken by or for the Government of India, should be couched in the fullest possible form and published at frequent and regular intervals. The financial position of India is such that she has nothing to fear from publicity; publicity is the great instrument through which to strengthen her credit abroad, and the position of the Government of India at home. *Magna est veritas et proevalebit*—but truth cannot prevail if it is interred in the archives of the India Office."

Ancillary Problems.

71. In my opinion the duty charged on silver imported into India is closely connected to deter the economic advancement of the people of India. This is a question which is not of importance so long as the embargo on private imports of silver is maintained, and no duty is consequently being levied. But when the embargo is raised I suggest that the duty should be given up because it is, in effect, a levy on the petty savings of multitudes of the people. The practice which custom impels the Indian masses to place such small cash reserves as they can scrape together in unfruitful investments in silver ornaments is, of course, a matter for regret, but it is simply a continuance of long established custom on the part of poor and ignorant classes whose individual accumulation are very small, and as a form of savings, not a fit subject for taxation.

72. It has to be remembered that the Indian masses were for long accustomed to see the values of silver, and of rupees on an equality. They could at any time convert their silver ornaments into rupees with little loss. With the closing of the Mints to the free coinage of silver this traditional equality of silver with rupees was broken.

Rupees became of less value than silver. That change by itself was startling enough to the poorer and uneducated classes, but while it had the effect of depreciating the value in rupees of their holdings of silver, it gave them the opportunity of putting future savings into the customary form of silver at an advantageous rate relatively to rupees. To this great change in the position of silver relatively to rupees there came to be added another innovation in the form of an import duty on silver, which meant that everyone who followed the usual custom of purchasing silver, was called upon to pay a contribution to the State. The amount of the duty is a minor consideration. It is the fact of the duty being levied which is objectionable, for if the principle of a duty is admitted there is always the risk of the duty being expanded, and that has already happened.

73. The great alteration caused in the rupee valuation of silver by the change in the monetary standard from silver to gold followed by the duty on silver imports, cut right into the established traditions and habits of the masses in the matter of their savings; and while there was good reason for the change in the standard there seems to me to be no sufficient reason for the silver duty. It is not calculated to inspire the masses with a sense of fairness on the part of Government towards their monetary habits, and on that account, is, I consider, likely to retard their economic advancement on sounder lines.

74. The duty on silver as carried out in practice is objectionable in other ways. When imported silver is re-exported the duty paid on importation cannot be recovered in full, thus placing an unfair burden on the Indian purchaser. In consequence of this inability to recover the duty in full on re-exports, the Indian silver market is placed at a disadvantage in competition with silver markets elsewhere, leading frequently to silver being retained in India when it might be re-exported. This disadvantage to the market reacts on holders of silver when they have occasion to dispose of their holdings, because, although they have paid the duty at the time of purchase, they may find when they come to sell that purchasers will deduct the duty from the market price on the ground that the silver may have to be sold abroad in competition with other silver markets.

India's Banking Problem.

75. India has an area of 1,802,657 square miles, and it contains 2,253 towns with 29,740,228 inhabitants and 720,342 villages with a population of 285,406,168. On the 31st December, 1917, the total number of banking offices in India was only 402, and many of them overlapped in the larger towns. In fact, on that date there were in the whole of India only 165 towns which had bank offices. The United Kingdom, with a population of 48,000,000, had 9,138 banking offices. Canada, with a population of 8,460,000, has about 4,000 branches of banks. Further, there are 294,875,000 illiterate people in India, and out of the 18,539,578 literates there are only 1,670,387 literates in English.

76. The vast and scattered population of India has thus modern banking facilities at 165, stations only, and consequently the financial power of India is insufficiently mobilised. Money lies dormant in endless small hoards.

77. It will be seen that there is a vast virgin field for the development and expansion of banking and for the collection into bank reserves of the innumerable stores of money lying idle throughout the country which could be utilised for the benefit of the holders and for the good of trade and of the State. At the same time expansion must necessarily be slow. The Indian public cannot be hurried and hustled in such matters.

78. It is sometimes said that a greater development of banking would cure the currency troubles. That seems to me to be putting the cart before the horse. The first essential to a great extension of modern banking is a currency system which inspires the public with absolute confidence. A credit system cannot overcome the difficulties arising from a system of money which is liable to violent changes in the valuation of the different forms of money of which it is composed, such as the present alteration in the ratio of rupees to the sovereign. No credit system could cure that fault in the money on which it rests. On the contrary, unsound money would imperil the credit system. Hence, in my opinion, the need for making the money system in India a specially strong and sound one if the money resources of India are ever to be mobilised in a great banking system.

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